18

TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1934

No. 338

DAVID H. JENNINGS, RECEIVER OF THE NATIONAL BANK OF AMERICA, AND NATIONAL BANK OF AMERICA, PETITIONERS,

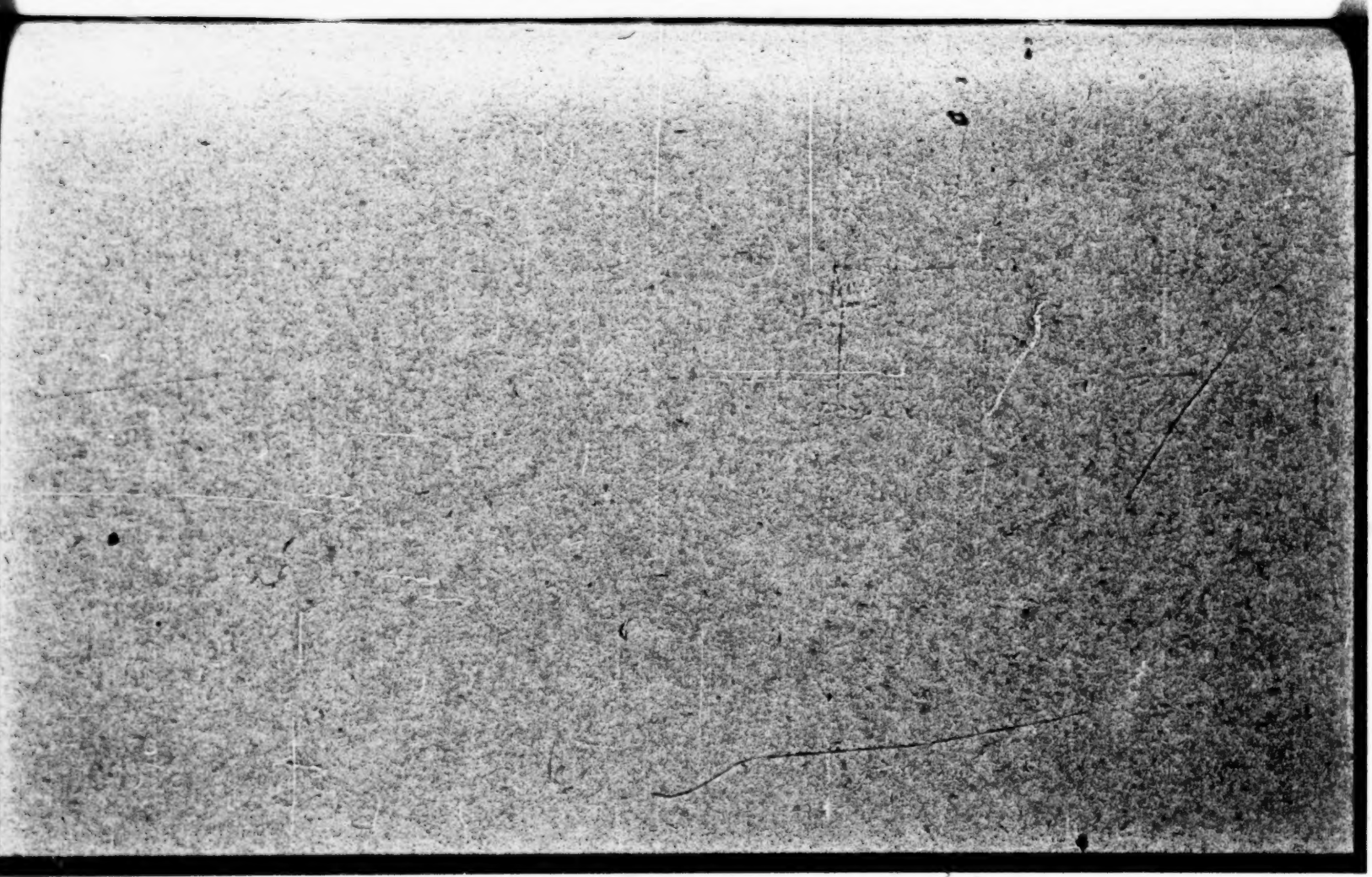
vs.

UNITED STATES FIDELITY AND GUARANTY COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

PETITION FOR CERTIORARI FILED AUGUST 31, 1934.

CERTIORARI GRANTED OCTOBER OCTOBER 8, 1934.



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IN THE DISTRICT COURT OF THE UNITED STATES

Placita.

Fort the Northern District of Indiana,

Hammond Division.

Pleas and Proceedings of the District Court of the United States for the Northern District of Indiana, Hammond Division, begun and holden at the United States Court House in the City of Hammond, in said district, at the March Term, 1932, of said court, before the Honorable Thomas W. Slick, Judge of said court.

United States Fidelity and Guaranty Company, a corporation,
vs.
National Bank of America, a corporation; David H. Jennings, as Receiver of National Bank of America. } Law 538.

Be It Remembered, that heretofore, to-wit, at the March Term, 1932, of said court, on the 24th day of October, 1932, the defendant by its attorneys, McMahon & Smith, filed in the office of the Clerk of this court, transcript on removal from the Lake Circuit Court, Crown Point, Indiana, which transcript contained bill of complaint, petition to remove from the Lake Circuit Court of Indiana to the United States District Court for the Northern District of Indiana, notice of filing of petition to remove and acknowledgment of service, bond for removal, which read in the words and figures following, to-wit:

2 State of Indiana } ss.
County of Lake }

plaint filed
t. 24, 1932.

IN THE LAKE CIRCUIT COURT

September Term, 1932

United States Fidelity and Guaranty Company, a corporation,
Plaintiff,
vs.
National Bank of America, a corporation, David H. Jennings, as Receiver of National Bank of America,
Defendants.
} Cause No. 23265.

COMPLAINT.

United States Fidelity and Guaranty Company, plaintiff herein, complains of the above-named defendants and for its cause of action against said defendants alleges:

That plaintiff is a corporation organized under the laws of the State of Maryland and is engaged in the business of surety for hire and of insuring against casualties; that plaintiff has been duly admitted to do business in the State of Indiana and is duly licensed to carry on said business in said State.

That defendant National Bank of America is a national banking association organized under the national bank Act of the United States, and defendant David H. Jennings, is the receiver thereof under appointment by the Comptroller of the Currency of the United States.

That on the ..... day of December 1931 plaintiff received a check for the sum of $2196.89, payable to it, from Com-
3 mercial Trust Company of Gary Indiana, drawn by said Trust Company upon the Gary State Bank of Gary, Indiana:

That on or about the 29th day of December, 1931, plaintiff deposited said check for collection with Security Trust Company of Indianapolis, Indiana, as agent for plaintiff, which last named Trust Company turned said check over to Fletcher American National Bank of Indianapolis, Indiana as sub-agent for collection; that said last named bank turned

said check over to defendant National Bank of America as sub-agent of plaintiff's said agent for collection in plaintiff's behalf:

That defendant National Bank of America presented said check to said drawee bank and received payment therefor in said sum of $2196.89 from said drawee bank and forwarded said sum on the ..... day of January, 1932 to Fletcher American National Bank of Indianapolis, Indiana, from which last mentioned bank said defendant bank had received said check for collection:

That soon thereafter, defendant, David H. Jennings, was duly appointed receiver of defendant National Bank of America by the Comptroller of Currency of the United States and is now such receiver; that said receiver demanded of said Fletcher American National Bank the return of said sum of $2196.89 so collected and forwarded by defendant National Bank of America, and said Fletcher American National Bank did pay over said sum so received by it to said receiver who has ever since held said sum. That said sum when so collected by defendant National Bank of America was held by it in trust for plaintiff and was forwarded by it as such trustee to said Fletcher American National Bank, which bank also held the same in trust for plaintiff; that when said sum was paid to said receiver by said Fletcher American National Bank the same was a trust fund in plaintiff's favor and
4 that defendant National Bank of America had no interest therein or right thereto and that said receiver had no interest therein and no right thereto; that said sum in said receiver's hands constitutes trust funds in favor of plaintiff and at all times were and now are, exclusively the property of plaintiff and at no time constituted assets of said defendant bank.

That plaintiff has made demand on defendants for said sum so received and held by them, but that each of defendants refused and still refuse to pay the same over to plaintiff. That plaintiff is entitled to have said sum paid to it by said receiver in full before said receiver pays any sums to creditors of defendant bank out of the assets of said bank, together with interest thereon since the ..... day of January, 1932.

That defendant receiver refuses to allow and pay plaintiff's said claim as a claim entitled to preferred payment over the general creditors of defendant bank, and that defendant bank by and through said receiver and the said receiver will, unless enjoined from so doing, wrongfully treat

said trust fund as constituting assets of defendant bank and will wrongfully apply the same to the payment of the expenses of said receivership and will wrongfully distribute the same, after the payment of receivership expenses, ratably among the creditors of defendant bank; that the assets of defendant bank together with the said trust fund would not be sufficient to pay plaintiff's said claim in full if said claim were allowed as a general claim and if it would participate ratably with other general creditors in the distribution thereof; that unless defendants are enjoined from doing the wrongful acts aforesaid plaintiff will suffer irreparable damage.

5 That plaintiff is entitled to an injunction against defendants enjoining them from using said trust fund as assets of defendant bank or of said receivership for the payment of said receivership expenses or for distribution among the creditors of defendant bank and enjoining defendants from making any payments to general creditors of defendant bank until after they shall have first paid plaintiff in full the amount of said trust fund, and plaintiff is entitled to a decree adjudging that plaintiff shall recover from defendants the said sum of $2196.89 with interest thereon forthwith and before defendants make any payments to such general creditors.

That plaintiff has no adequate remedy at law in the premises.

Wherefore, plaintiff prays that defendants each be permanently enjoined from using any part of said trust fund as assets of defendant bank or of said receivership for the payment of receivership expenses or for distribution among the creditors of defendant bank and from making any payments to general creditors of defendant bank until after they shall have first paid plaintiff in full the amount of the said trust fund; plaintiff further prays that the court adjudge and decree that plaintiff shall recover from defendants the said sum of $2,196.89 with interest thereon and that defendants shall pay the same to plaintiff forthwith and before they make any payments to general creditors of defendant bank; plaintiff further prays that it recover its costs laid out and expended in this action, and for all other proper relief in the premises.

PICKENS, DAVIDSON, GAUSE, GILLIOM & PICKENS,
ARTHUR L. GILLIOM,
Attorneys for Plaintiff.

6 State of Indiana, } ss:
County of Lake. }

IN THE LAKE CIRCUIT COURT,

Petition f
Removal

Sitting at Crown Point,

September Term, 1932.

United States Fidelity and Guaranty Company, a corporation,
vs.
National Bank of America, a corporation, and David H. Jennings, as Receiver for the National Bank of America. } Cause No. 23265.

PETITION OF DEFENDANTS TO REMOVE CAUSE TO THE UNITED STATES DISTRICT COURT FOR THE HAMMOND DIVISION OF THE NORTHERN DISTRICT OF INDIANA.

Come now the National Bank of America and David H. Jennings, as Receiver of the National Bank of America, defendants in the above entitled cause and respectfully show to this honorable court that this is an action commenced against these petitioners by the filing of a complaint in the Circuit Court of Lake County, state of Indiana, and the issuing of a summons to these defendants to appear in court on the third day of October, 1932, to answer said complaint of the plaintiff, United States Fidelity and Guaranty Company, a corporation.

The plaintiff's alleged cause of action as set forth in said complaint, is to recover a judgment against these defendants for the sum of Two Thousand One Hundred Ninety Six and 89/100 ($2,196.89) Dollars, with interest thereon from the ..... day of January, 1932, which said sum it is alleged the defendant, National Bank of America, collected for the plaintiff herein and which the said defendant bank
7 held in trust for the plaintiff herein, and which sum the said plaintiff asks may be allowed as a preferred claim against the said defendants, it being alleged in said complaint that in December, 1931, the plaintiff received a check for $2,196.89, payable to it from the Commercial Trust Com-

pany of Gary, Indiana, drawn by said trust company upon The Gary State Bank, of Gary, Indiana.

That plaintiff deposited said check for collection with the Security Trust Company of Indianapolis, as agent for plaintiff and said last named trust company turned said check over to the Fletcher American National Bank of Indianapolis as sub-agent. That said last named bank turned said check over to the defendant, National Bank of America, as sub-agent of plaintiff, for collection in plaintiff's behalf. That the defendant, National Bank of America, presented said check to The Gary State Bank and received payment therefor in the sum of $2,196.89, and forwarded said sum, on the ..... day of January, 1932, to the Fletcher American National Bank of Indianapolis, Indiana.

That soon thereafter the defendant and petitioner herein, David H. Jennings, was duly appointed receiver of said National Bank of America by the Comptroller of the Currency of the United States and is now such receiver.

That said receiver demanded of said Fletcher American National Bank the return of said sum of $2,196.89 so collected and said Fletcher American National Bank did return and pay over said sum so received by it to the said David H. Jennings, as Receiver of said National Bank of America, who ever since, has held said sum. That said sum, when collected by the defendant, National Bank of America, was held by it in trust for plaintiff, and that neither the defendant
National Bank of America, nor the defendant, David H.
8 Jennings, as receiver of said bank, has any interest
therein or right thereto, and that said sum in the hands of said receiver constitutes a trust fund in favor of the plaintiff, United States Fidelity and Guaranty Company. That the plaintiff has demanded that said receiver pay said sum over to the plaintiff, but that said receiver refuses to allow and pay said claim as a claim entitled to preference over the general creditors of the National Bank of America.

Your petitioners further show that the defendant, National Bank of America, is a corporation organized under the laws of the Congress of the United States and as such was, on January, 2, 1932 and for many years prior thereto, engaged in the banking business in the city of Gary, Lake county, Indiana. That the said National Bank of America became insolvent, and on January 4, 1932, the Comptroller of the Currency of the United States took possession of said last named bank and its assets, and that thereafter, to-wit: on the 10th day of February, 1932, the said Comptroller of the Currency appointed

the defendant, David H. Jennings, as receiver for the said National Bank of America for the purpose of administering its assets and closing up its business affairs, and that he is now the duly acting and qualified receiver of said bank by virtue of an appointment from the Comptroller of the Currency of the United States of America.

Your petitioners further show to the court that plaintiff's alleged cause of action and the controversy herein between the plaintiff and these petitioners is an action against a bank organized under the laws of the United States, to-wit: the National Bank of America; that it is a case which relates
9 to the winding up of the affairs of said insolvent National Bank of America and that it is an action brought against an officer and agent of the United States; namely, David H. Jennings, Receiver of said National Bank of America and is an action arising under the laws of the United States of America and that it is the desire of your petitioners to remove said cause from this honorable court to the United States District Court for the Hammond Division of the Northern District of Indiana, in accordance with the provisions of the acts of Congress of the United States in that behalf and provided.

Your petitioners file and offer herewith bond with good and sufficient security as required by law, for its entering into the United States District Court, Hammond Division of the Northern District of Indiana, within thirty days of the filing of said petition, a certified copy of the record in said suit and for paying all costs that may be awarded by the said District Court of the United States for the Hammond Division of the Northern District of Indiana, if said District Court shall hold that such suit was wrongfully and improperly removed thereto and also for its appearing and entering special bail in such suit, if such special bail was originally requisite therein according to the provision of the Act of Congress in such case made and provided.

Your petitioners further show that written notice of this petition and said bond for removal was given to the plaintiff herein prior to the filing of this petition, by service of notice and a copy of this petition and said bond upon said attorneys of record in this case, on the 30th day of September, 1932.

That by reason of the facts aforesaid, these petition-
10 ers are entitled to removal of this suit to the United States District Court for the Hammond Division of the Northern District of Indiana.

Wherefore, petitioners pray the court to proceed no fur-

ther herein except to make an order of removal, as required by law, and to accept said surety and bond and cause the records hereof to be removed to the United States District Court for the Hammond Division of the Northern District of Indiana, and for all other proper relief in the premises.

McMAHAN & SMITH
Attorneys for the Defendants, National Bank of America, and David H. Jennings, Receiver for the National Bank of America.

11 State of Indiana } ss:
County of Lake }

IN THE LAKE CIRCUIT COURT

Sitting at Crown Point

September Term, 1932.

United States Fidelity and Guaranty Company, a corporation
vs.
National Bank of America, a corporation, and David H. Jennings, as Receiver for the National Bank of America. } Cause No. 23265

AFFIDAVIT.

WILLIS C. McMAHAN, being duly sworn upon his oath deposes and says that he is one of the attorneys for the National Bank of America and for David H. Jennings, receiver of the National Bank of America, the defendants in the above entitled cause, and has authority to make and does make this affidavit for and on behalf of said defendants and each of them.

That he has read the foregoing petition, knows the contents thereof, and says that said petition is true to the best of his knowledge and belief.

(Signed) WILLIS C. McMAHAN

Subscribed and Sworn to before me this 28th day of September, 1932.

(Signed) JEANNETTE EMMETT
Notary Public

My commission expires: Sept 25 1935.

12 State of Indiana } ss:
County of Lake }

IN THE LAKE CIRCUIT COURT

Bond on Removal.

Sitting at Crown Point

September Term, 1932.

United States Fidelity and Guaranty Company, a corporation
vs.
National Bank of America, a corporation, and David H. Jennings, as Receiver for the National Bank of America.

BOND ON REMOVAL.

Know All Men By These Presents: That David H. Jennings, as Receiver for the National Bank of America, as principal, and the National Surety Company of New York, a corporation duly organized and existing under and by virtue of the laws of the state of New York, and having authority to transact business in the state of Indiana, as surety, are held and firmly bound unto the United States Fidelity and Guaranty Company, a corporation, in the sum of Five Hundred ($500.) Dollars, for the payment of which well and truly to be made unto the said United States Fidelity and Guaranty Company, to said David H. Jennings, as Receiver of the National Bank of America, and the National Surety Company of New York bind themselves, their successors and assigns, jointly and firmly by these presents.

The condition of this obligation is such that:

Whereas, the above named United States Fidelity and Guaranty Company has heretofore brought a suit of a civil nature in the Lake Circuit Court of the state of Indiana, against the National Bank of America and David H.
13 Jennings, as Receiver of the National Bank of America; and

Whereas, the said defendants, National Bank of America and David H. Jennings, as Receiver of the National Bank of America, simultaneously with the filing of this bond, intend to file their petition in said suit in such state court for the

removal of such suit into the District Court of the United States for the Hammond Division of the Northern District of Indiana, according to the provisions of the Act of Congress in such cases made and provided.

Now, therefore, the condition of this obligation is such that if said petitioners, the National Bank of America and David H. Jennings, as Receiver for the National Bank of America, shall enter in the District Court of the United States for the Hammond Division of the Northern District of Indiana within thirty days of the filing of said petition, a certified copy of the record in such suit and for paying all costs that may be awarded by the said District Court if said District Court shall hold that said suit was wrongfully or improperly removed thereto, and also for appearing and entering special bail in such suit, if special bail was originally requisite therein, then the above obligation shall be void, but shall otherwise remain in full force and effect.

In Witness Whereof, David H. Jennings, as Receiver of the National Bank of America, and the said National Surety Company of New York has caused this instrument to be signed by its duly authorized agents and officers and its corporate seal to be hereunto affixed this 29th day of September, 1932.

(Signed) DAVID H. JENNINGS
David H. Jennings,
Receiver for National Bank of America, Principal

14 NATIONAL SURETY COMPANY OF NEW YORK,
By J. BOROWSKI
J. Borowski
(Seal) *Resident Vice-President, Surety*
Attested:
D. L. SHEARER
D. L. Shearer
Resident Assistant-Secretary

15 And afterward, to-wit, at the March Term, 1933, of said court, and on the 15th day of May, 1933, before the Honorable Thomas W. Slick, Judge of said court, the following further proceedings were had in said cause, to-wit:

Come now the parties herein and file stipulation for transfer of this cause to the South Bend Division of this court, which stipulation reads in the words and figures following, to-wit:

16 IN THE DISTRICT COURT OF THE UNITED STATES Filed May 1933.

For the Northern District of Indiana

Hammond Division

United States Fidelity and Guaranty Company, a corporation
vs.
National Bank of America, a corporation, and David H. Jennings, as Receiver for the National Bank of America. } Law No. 538

Comes now the above named plaintiff by its attorneys, Pickens, Davidson, Gause, Gilliom and Pickens, and come also the defendants by their attorneys, McMahan & Smith, and stipulate and agree that this cause may be transferred from the Hammond Division of said court to the South Bend Division of said court, and the said plaintiffs and the said defendants hereby consent that the court make and enter of record an order transferring this cause to the South Bend Division of said court.

PICKENS, DAVIDSON, GAUSE, GILLIOM AND PICKENS,
Attorneys for Plaintiff.
McMAHAN & SMITH
Attorneys for Defendants.

17 And thereupon, the following further proceedings were had in said cause, to-wit:

Come now the defendants and files its answer in one paragraph, which answer reads in the words and figures following, to-wit:

18 • • (Caption) • •

ANSWER.

Come now the defendants, National Bank of America and David H. Jennings, as Receiver for the National Bank of America, and for answer to the plaintiff's complaint, admit

that the plaintiff is a corporation organized under the laws of the state of Maryland and is engaged in the business of surety for hire and of insuring against casualties. That plaintiff has been admitted to do business in the state of Indiana and is duly licensed to carry on said business in this state.

That the defendant, National Bank of America, is a banking association organized under the National Banking Act of the United States and that the defendant, David H. Jennings, is the receiver of said National Bank of America under appointment by the Comptroller of the Currency of the United States.

That the plaintiff, in December, 1931, received from the Commercial Trust Company of Gary, Indiana, a check for the sum of Two Thousand One Hundred Ninety Six and 89/100 ($2,196.89) Dollars, payable to the plaintiff and drawn by said trust company upon the Gary State Bank. That on the 31st day of December, 1931, the defendant National Bank of
19 America received said check from the Fletcher American National Bank of Indianapolis, Indiana, for collection and remittance.

The defendants, further answering, say that on January 2, 1932, and for more than five years prior thereto, there was an organization in the city of Gary, Indiana, known as the Gary Clearing House Association organized by and comprised of the banks doing business in the said city of Gary, and which association was organized for the purpose of facilitating the exchange of checks and settling the balances with and among the several members of said association. That during all the time mentioned in this answer and during the time mentioned in the complaint herein, the National Bank of America, the First National Bank of Gary, and the Gary State Bank were members of said clearing house association. That on December 31, 1931, and on January 2, 1932, the said National Bank of America, the First National Bank of Gary, and the Gary State Bank were the sole and only members of the said clearing house association.

That on January 2, 1932, and for several years prior thereto it was the custom and practice of the banks which were members of said clearing house association to have a representative of and from each of said banks meet a representative from each of the other member banks of said association at the rooms and office of said association at ten o'clock a. m., of every business day, for the purpose of exchanging checks received by each of said members before nine thirty o'clock

a. m., of that day, and which were drawn upon the various banks which were then members of said association, for the purpose of exchanging such checks so drawn upon and
20 against the several members of said association and settling the accounts of said banks with each other. That it was the custom of said banks and of said association when, upon the presentation and exchange of checks by said members banks to and through said association, it was found that the checks drawn on any of said banks and presented for payment through the clearing house association exceeded the amount of the checks drawn on other member banks and which such other banks held, for the debtor bank to pay such difference to the clearing house association by the draft of such debtor bank drawn upon its correspondent bank in the city of Chicago, Illinois, after which the said clearing house association would distribute such difference to the member banks entitled thereto.

The defendants, further answering, say that prior to nine thirty o'clock a. m., of December 31, 1931, the said National Bank of America received from the Fletcher American National Bank of Indianapolis, Indiana, for collection, checks drawn on other banks in Gary aggregating in the sum of $3,661.83, including said check for $2,196.89, drawn by the Commercial Trust Company of Gary on the Gary State Bank. That in addition to said check for $2,196.89, the said National Bank of America, at said time, had received other checks drawn on the Gary State Bank in the sum of Five Thousand Eight Hundred Ninety eight and 67/100 ($5,898.67) Dollars. That the said National Bank of America also, at said time, had received in the usual course of business, checks drawn on the First National Bank of Gary in the aggregate sum of Two Thousand Three Hundred Twenty nine and 89/100 ($2,329.89) Dollars, making a total of Ten Thousand Four Hundred Twenty five and 45/100 ($10,425.45) Dollars of checks so held by the National Bank of America and drawn on the other two members of said
21 clearing house association, and which were, on said 31st day of December, 1931, presented by said National Bank of America to the said clearing house association for exchange and clearance.

That the other member banks of said association; namely, the Gary State Bank and the First National Bank of Gary, on said day held and presented to the said clearing house association checks drawn on said National Bank of America

in the sum of Eleven Thousand Four Hundred Seventy and 19/100 ($11,470.19) Dollars. That as a result of said clearings and exchange of checks on the morning of said 2nd day of January, 1932, the said National Bank of America was indebted to and owed the clearing house association the sum of One Thousand Forty four and 75/100 ($1,044.75) Dollars for which said last named sum the National Bank of America drew its check or draft on the Continental Illinois Bank and Trust Company of Chicago, Illinois, payable to the order of said clearing house association and delivered said check to the said clearing house association in settlement of the said sum of $1044.75 which said National Bank of America owed said clearing house association, and that the assets and funds of the National Bank of America were not increased or augmented by reason of the collection of said check of $2,196.89 so received from the Fletcher American National Bank of Indianapolis, Indiana.

The defendants, further answering the plaintiff's complaint, say that they are not advised as to the relation existing between the Fletcher American National Bank of Indianapolis and the plaintiff, United States Fidelity and Guaranty Company, and do not know whether the said check for $2,196.89 drawn by the Commercial Trust Company of Gary, Indiana, on the Gary State Bank was owned by the Fletcher American National Bank or whether, when said last
22 named bank sent said check to the National Bank of America, it was acting as an agent for plaintiff in so sending said check to the National Bank of America.

And further answering said complaint, the defendants say that the said National Bank of America, in collecting said check for the said Fletcher American National Bank of Indianapolis, was acting as the agent of the said last named bank. That for several years prior to the 2nd day of January, 1932, it was the custom of said Fletcher American National Bank to send checks drawn on banks in the city of Gary, other than the defendant bank, to the said National Bank of America for collection. That during all of said time, as the said Fletcher American National Bank well knew, it was the custom of the National Bank of America to present such checks so drawn on the other member banks of the clearing house association in Gary to the said clearing house association for clearance and collection; that it was not, as said Fletcher American National Bank well knew, the custom of the National Bank of America to present the checks so

sent to it for collection, to the drawee bank and to receive from the drawee bank money in payment thereof; that on December 31, 1931, and for a long time prior thereto, it was the custom of the National Bank of America, as the Fletcher American National Bank well knew, when collection of such checks was made through the clearing house association, for the said National Bank of America to draw its check or draft in favor of the said Fletcher American National Bank on a correspondent bank of the National Bank of America and to send such check or draft to the said Fletcher American National Bank in payment of the collection so made.

And the said defendants, further answering the plain-
23 tiff's complaint, admit that the National Bank of America was, at the time when it ceased doing business, indebted to the owner of the said check for $2,196.89, in the sum of $2,196.89, and that the owner of said check is entitled to have the amount of said check allowed and paid as a general claim without any preference over other general creditors of the National Bank of America, but defendants deny each and every allegation of plaintiff's complaint not herein admitted, and say that plaintiff's alleged claim is not, and should not be allowed as preferred.

Wherefore, the defendants pray that this honorable court adjudge and decree that the claim of the plaintiff be not allowed and ordered paid as a preferred claim.

McMahan & Smith,
Attorneys for Defendants.

24 And thereupon, the following further proceedings were had in said cause, to-wit:

And now the plaintiff offers in evidence PLAINTIFF'S EXHIBIT 1, being stipulation of facts, as evidence, which Exhibit 1 is now admitted in evidence, and reads in the words and figures following, to-wit:

(The stipulation of facts was incorporated by the court in the Special Finding of Facts, and is copied in full and set out on pages 26 to 41 of the transcript.)

Sept. 13, 3. 25 * * (Caption) * *

ENTRY FOR SEPTEMBER 13, 1933.

Comes now Thomas W. Slick, Judge of the District Court of the United States for the Northern District of Indiana, and assumes the bench, and the following proceedings were had in the above entitled cause:

The Court having heard the evidence consisting wholly of a written stipulation of facts entered into by the parties hereto and being designated as plaintiff's exhibit No. 1, and having heard the argument of counsel, and being sufficiently advised in the premises, now adopts said stipulation of facts as and for its special finding of facts, and signs and files its special findings of fact and conclusions of law thereon, which said special findings of fact and conclusions of law are as follows, to-wit:

26 * * (Caption) * *

FINDINGS OF FACT.

The court finds specially the facts as follows, the same being stipulated by the parties, to-wit:

27 * * (Caption) * *

STIPULATION OF FACTS.

The plaintiff, by Arthur L. Gilliom, its attorney, and the defendants, by Willis C. McMahan and J. Edwin Smith, their attorneys, stipulate that the following facts are true and shall constitute the evidence in this cause:

1.

Plaintiff, United States Fidelity and Guaranty Company, is a corporation organized under the laws of the State of Maryland and is engaged in the business of surety for hire and of insuring against casualties; that plaintiff has been duly admitted to do business in the State of Indiana and is duly licensed to carry on said business in the State of Indiana; that plaintiff's principal office and place of business is in Baltimore, Maryland, and that during all of the times

herein mentioned plaintiff maintained an office in the city of Indianapolis, Indiana.

2.

The defendant, National Bank of America, is a National Banking association organized under the National bank act of the United States, and as such was, on January
28 2, 1932, and for many years prior thereto, continuously engaged in the general banking business in the City of Gary, County of Lake, State of Indiana; that the 1st day of January 1932 was New Years day and a National holiday and said bank was not open for business on that day; that said bank was open on Saturday, January 2nd, 1932, and did a regular banking business on that day until one o'clock in the afternoon, that being the regular closing hour for said bank on Saturdays; that said bank never opened for business after one o'clock of the afternoon of January 2nd, 1932; that on Sunday January 3rd, 1932 the directors of said bonk held a meeting and adopted a resolution to the effect that said bank should not open for business the following Monday, January 4, 1932, and on said 3rd day of January said board of directors notified the Chief National Bank Examiner for the Seventh Federal Reserve District of the adoption of said resolution. That on January 4, 1932, at about eight A. M., the Comptroller of Currency of the United States, through the National Banking Department and by F. F. Robinson, a deputy national bank examiner, took charge of said bank, and thereafter had continuous charge thereof until the defendant receiver took charge thereof on the 10th day of February 1932; that said receiver has been in continuous charge of said bank ever since said 10th day of February, 1932.

That said bank was insolvent on the fourth day of January, 1932, and has ever since then been insolvent; that the assets of said bank have at no time since its insolvency been sufficient to pay all of its debts in full, nor will they be; that on the 4th day of January, 1932, the Comptroller of the Currency of the United States took possession of said bank and of its assets, and said bank has not engaged in the banking business since then.

29 3.

The defendant, David H. Jennings, was duly appointed as receiver of said National Bank of America on the 10th

day of February, 1932 by the said Comptroller of the Currency for the purpose of administering its assets and closing up its business affairs, and that he has ever since been, and now is, the duly acting and qualified receiver of said bank in virtue of his said appointment from said Comptroller of the Currency of the United States.

4.

On the 30th day of December, 1931, plaintiff, United States Fidelty and Guaranty Company, received from Commercial Trust Company of Gary, Indiana, a check for the sum of $2196.89, dated December 29, 1931, payable to the order of plaintiff, which check was drawn by said Commercial Trust Company, as drawer, on the Gary State Bank of Gary, Indiana, as drawee. Said check was given to plaintiff, as aforesaid, in payment of an amount in the sum of said check then owing to plaintiff by said Commercial Trust Company on account of bond and insurance premiums collected by said Trust Company for the plaintiff.

5.

On the 30th day of December, 1931, plaintiff endorsed said check, which endorsement is as follows:

"Pay to the order of
Security Trust Company
Indianapolis
90 Prior endorsements guaranteed 90
United States Fidelity and Guaranty Co.
Foster & Messick, Mgrs."

On said last mentioned day plaintiff deposited said
30 check so endorsed, along with several other checks the aggregate amount of all of which checks was $10,927.31, with Security Trust Company of Indianapolis, Indiana. Said Security Trust Company was then a trust company organized under the laws of Indiana doing a general banking business under the laws of Indiana at said City of Indianapolis.

The manner in which said deposit of said check was made is as follows:

Plaintiff tabulated the amounts of said checks, including said check for $2,196.89, on adding machine tape with an adding machine and stamped its name, United States Fidelity and Guaranty Company on said tape ahead of the tabulated amounts of said checks, and immediately under-

neath said name plaintiff wrote the date "12-30-31". Said tape bearing said name, date and tabulated amounts of said checks was then pinned by plaintiff to a printed form of deposit slip furnished by said Security Trust Company to its depositors for use in making deposits in said Security Trust Company, which form of deposit slip and the printed matter thereon were as follows:

31 "No. ..... Credit Account of

.....

(Name of Depositor)
Security Trust Company
Indianapolis, ... 193....

Items other than currency on this slip credited only for collection at the depositor's risk, whether collected directly or indirectly. Please list each check separately

	Dollars	Cents
Currency	.....	.....
Gold	.....	.....
Silver	.....	.....
Checks as follows	.....	.....
. . ..	.....	.....
. . ..	.....	.....
. . ..	.....	.....
. . ..	.....	.....
. . ..	.....	.....
. . ..	.....	.....
. . ..	.....	.....
. . ..	.....	.....
Total $	.....	.....

See that all checks and drafts are endorsed"

32 Thereupon, on said 30th day of December, 1931 plaintiff delivered said tabulated checks, including said check of $2,196.89 from Commercial Trust Company, together with said deposit slip and attached tape bearing said name, date and tabulated amounts of said checks, to said Security Trust Company and received on said day a credit to its, plaintiff's account with said Security Trust Company in said total sum of $10,927.89 because of deposit of said checks, including said check for $2,196.89.

6.

Thereupon, on or about the 30th day of December, 1931, said Security Trust Company endorsed said check for $2,196.89 issued by Commercial Trust Company and so de-

posited by plaintiff and deposited the same on said day to its account with Fletcher American National Bank of Indianapolis, Indiana and then received credit in the sum of said check from said Fletcher American National Bank; that said endorsement is as follows:

"Pay to the order of
any bank, banker or trust Co.
20-11 Security Trust Co. 20-11
C Indianapolis, Ind.
Wm. C. Kassebaum, Secy.
Dec. 31, 1931"

Said Fletcher American National Bank was then a national bank doing a general banking business in the City of Indianapolis, Indiana.

In depositing said check in Fletcher American National Bank on December, 30, 1931, said Security Trust Company made out a deposit slip on the printed form regularly used at said Fletcher American National Bank and delivered the same with the checks, including said check for
33 $2,196.89, deposited by it in Fletcher American National Bank on that day. At the time said deposit slip was so delivered, there was pinned thereto on a separate piece of paper a tabulated list of the checks being deposited and aggregating the sum of $176,962.39 shown on said deposit slip, including said check for $2,196.89. Said deposit slip so made out and delivered was as follows:

34 "Deposited for the Account of
Security Trust Company

The Fletcher American National Bank of Indianapolis	With the Fletcher American National Bank	The Fletcher American National Bank of Indianapolis

Indianapolis, Dec 30 1931 19.....

In receiving items, this bank acts only as the depositor's collecting agent and assumes no responsibility for loss in the mails, or through the failure of any direct or indirect collecting agent. Until actual funds or solvent credits have come into its possession this bank reserves the right to charge to the depositor's account any amount so credited. Checks on

this bank are credited subject to their being good when charged in the ordinary course of business.

	Dollars	Cents
Currency		
Gold		
Silver		
Checks	176,962	39
14 Dec 30 1931		
Total		

35 Thereupon, on or about the 30th day of December, 1931 said Fletcher American National Bank endorsed said check as follows:

"Pay any bank or banker or order
Prior endorsements guaranteed
14 Dec 30 1931 14
The Fletcher American Natl. Bank
of Indianapolis
20-1 Ralph K. Smith 20-1
Vice-Pres. & Cashier"

Said check so endorsed was then mailed, on or about the 30th day of December, 1931, by said Fletcher American National Bank to its correspondent bank the National Bank of America at Gary, Indiana for collection from said drawee Gary State Bank, and for remittance to said Fletcher American National Bank, and said check was received for said purposes by National Bank of America in the morning of December 31, 1931.

8.

On January 2, 1932, and for more than five years prior thereto, there was an organization in the city of Gary, Indiana, known as the Gary Clearing House Association organized by and comprised of the banks doing business in the said city of Gary, and which association was organized for the purpose of facilitating the exchange of checks and settling

the balances with and among the several members of said association. That on and prior to said last named day, the National Bank of America, the First National Bank of Gary, and the Gary State Bank were members of said clearing house association. That on December 31, 1931, and on January 2, 1932, the said National Bank of America, the First
36 National Bank of Gary, and the Gary State Bank were the sole and only members of the said clearing house association.

That on January 2, 1932, and for several years prior thereto it was the custom and practice of the banks which were members of said clearing house association to have a representative of and from each of said banks meet a representative from each of the other member banks of said association at the rooms and office of said association at ten o'clock a. m., of every business day, for the purpose of exchanging checks received by each of said members before nine thirty o'clock a. m., of that day, and which were drawn upon the various banks which were then members of said association, for the purpose of exchanging such checks so drawn upon and against the several members of said association and settling the accounts of said banks with each other. That it was the custom of said banks and of said association when, upon the presentation and exchange of checks by said member banks to and through said association, it was found that the checks drawn on any of said banks and presented for payment through the clearing house association exceeded the amount of the checks drawn on other member banks and which such other banks held, for the debtor bank to pay such difference to the clearing house association by the draft of such debtor bank drawn upon its correspondent bank in the city of Chicago, Illinois, after which the said clearing house association would distribute such difference to the member banks entitled thereto.

That prior to nine thirty o'clock a. m., of December 31, 1931, the said National Bank of America received from the Fletcher American National Bank of Indianapolis, Indiana, for collection, checks drawn on other banks in Gary aggregating in the sum of $3,660.83, including said check for
37 $2,196.89 drawn by the Commercial Trust Company of Gary on the Gary State Bank. That in addition to said check for $2,196.89, the said National Bank of America, at said time, had received other checks drawn on the Gary State Bank in the sum of Five Thousand Eight Hundred

Ninety-eight and 67/100 ($5,898.67) Dollars. That the said National Bank of America also, at said time, had received in the usual course of business, checks drawn on the First National Bank of Gary in the aggregate sum of Two Thousand Three Hundred Twenty-nine and 89/100 ($2,329.89), Dollars, making a total of Ten Thousand Four Hundred Twenty-five and 45/100 ($10,425.45) Dollars of checks so held by the National Bank of America and drawn on the other two members of said clearing house association, and which were, on said 31st day of December, 1931, presented by said National Bank of America to the said clearing house association for exchange and clearance.

That the other member banks of said association; namely, the Gary State Bank and the First National Bank of Gary, on said day held and presented to the said clearing house association checks drawn on said National Bank of America in the sum of Eleven Thousand Four Hundred Seventy and 19/100 ($11,470.19) Dollars. That as a result of said clearings and exchange of checks on the morning of said 31st day of December, 1931, the said National Bank of America was indebted to and owed the clearing house association the sum of One Thousand Forty-four and 75/100 ($1,044.75) Dollars for which said last named sum the National Bank of America drew its check or draft on the Continental Illinois Bank and Trust Company of Chicago, Illinois, payable to the order of said clearing house association and delivered said check to the said clearing house association in settlement of the said sum of $1,044.75 which said National Bank of
38 America owed said clearing house association.

National Bank of America would have owed and paid said clearing house the sum of $2,196,89 more than it did owe and pay said clearing house on December 31, 1931, if it had not received, presented and exchanged said check for $2,196.89 on said day.

Said drawee Gary State Bank received said check for $2,196.89 as a result of said clearing house transaction on said 31st day of December, stamped the same paid on said day, charged the account of drawer Commercial Trust Company with the amount thereof and delivered it stamped paid to said drawer.

9.

That for several years prior to the 2nd day of January, 1932, it was the custom of said Fletcher American National

Bank to send checks drawn on banks in the city of Gary, other than the defendant bank, to the said National Bank of America for collection. That during all of said time, as the said Fletcher American National Bank well knew, it was the custom of the National Bank of America to present such checks so drawn on the other member banks of the clearing house association in Gary to the said clearing house association for clearance and collection; that it was not, as said Fletcher American National Bank well knew, the custom of the National Bank of America to present the checks so sent to it for collection, to the drawee bank and to receive from the drawee bank money in payment thereof; that on December 31, 1931 and for a long time prior thereto, it was the custom of the National Bank of America, as the Fletcher American National Bank well knew, when collection of such checks was made through the clearing house association, for the said National Bank of America to draw its check or
39 draft in favor of the said Fletcher American National Bank on a correspondent bank of the National Bank of America and to send such check or draft to the said Fletcher American National Bank in payment of the collection so made.

When National Bank of America collected said checks drawn on Gary banks aggregating $3,660.83, including said check for $2,196.89 drawn on Gary State Bank, and while it was still conducting its regular banking business, it drew its draft dated December 31, 1931, on Continental Illinois Bank & Trust Company of Chicago, Illinois, payable to Fletcher American National Bank in said sum of $3,660.83 and mailed the same to Fletcher American National Bank at Indianapolis on the 31st day of December, 1931, in remittance of the amount collected by it upon said checks, including said check for $2,196.89. At said time National Bank of America had on deposit at said Continental Illinois Bank and Trust Company a sum greater than the amount of said draft.

10.

Fletcher American National Bank received said draft for $3,660.83 from National Bank of America on January 2nd, 1932, and on the same day it endorsed said draft and mailed the same to said Continental Illinois Bank and Trust Company for the purpose of receiving payment thereon.

Continental Illinois Bank and Trust Company received said draft at Chicago on January 4, 1932, by which time the

said National Bank of America had suspended business and was in charge of said Comptroller and Continental Illinois Bank and Trust Company for that reason refused to pay said draft and returned the same unpaid to Fletcher American National Bank at Indianapolis on January 4, 1932.

11.

40 At the time when said draft was received by Fletcher American National Bank from Continental Illinois Bank & Trust Company after payment thereof had been refused, and on the 5th day of January, 1932, said National Bank of America had on deposit to its account with Fletcher American National Bank the total sum of $3,994.74. On said 5th day of January, 1932, said Fletcher American National Bank charged on its books to the said account of National Bank of America the amount of said returned draft in the sum of $3,660.83. On March 3, 1932 Fletcher American National Bank paid to said receiver the balance, after said charge of $3,660.83, of said account of National Bank of America, and retained the amount so charged against said account because of said returned draft.

Thereafter, and prior to July 7, 1932, said receiver demanded of Fletcher American National Bank that it pay to him the amount of said draft so charged against said account of National Bank of America, and thereupon Fletcher American National Bank did, in compliance with said demand, pay said sum of $3,660.83 to said receiver on the 18th day of July, 1932.

12.

On July 7, 1932 Fletcher American National Bank charged the amount of said check for $2,196.89, which was included in said sum of $3,660.83, against said account of Security Trust Company, and said Security Trust Company did in turn on the 7th day of July, 1932, charge plaintiff's said account with said sum of $2,196.89 which it had originally credited to plaintiff's account at the time when said check was deposited as aforesaid.

Plaintiff's account with Security Trust Company has ever since remained diminished by the said amount of $2,196.89 so charged against it on the 7th day of July,
41 1932, and plaintiff has not received payment from anyone for any part of said check for $2,196.89 deposted by

it with Security Trust Company on said day of December, 1931.

13.

National Bank of America did not remit for the sum so collected by it through said clearing house upon said check for $2,196.89 drawn on, and paid by, said Gary State Bank otherwise than by means of said unpaid draft for $3,660.83 drawn by it on Continental Illinois Bank & Trust Company. Said unpaid draft was returned by Fletcher American National Bank to said receiver.

At the time said receiver took charge of National Bank of America there were in possession of said bank cash items in excess of $2,196.89. There have at all times been, and now are, in possession of said receiver cash items in excess of $2,196.89.

Plaintiff made demand before commencement of this suit upon said receiver for payment to it in full of said sum of $2,196.89 collected by said bank upon said check, but said receiver refused and still refuses to pay to plaintiff the same sum in preference over general claims. The receiver has at all times been, and now is, willing to pay upon said amount of $2,196.89 as a general claim ratable dividends as and when declared. Said receiver has at all times treated, and intends to treat, said sum of $2,196.89 as a part of the assets of said bank for ratable distribution among the creditors of said bank.

Signed on the 15th day of May, 1933.

(Signed) PICKENS, DAVIDSON, GAUSE, GILLIOM & PICKENS,
Attorney for Plaintiff.
McMAHAN & SMITH,
Attorneys for Defendants.

42 CONCLUSIONS OF LAW.

Upon the above special findings of fact as stipulated the court finds the following conclusions of law:

1.

That the cash items of defendant National Bank of America became impressed with a trust in plaintiff's favor in the sum of $2,196.89 at the time said check was collected by said National Bank of America, and the receiver Jennings took over said sum of money subject to said trust.

2.

That plaintiff is entitled to recover said sum of $2,196.89, together with interest at the rate of 6%, from the defendant receiver in preference to the general creditors of said bank.

3.

Plaintiff is entitled to recover its costs against the defendant in this action.

4.

In all respects the law is with plaintiff.

(Signed) THOS. W. SLICK,
Judge, U. S. District Court.

September 13, 1933.

43 And the same are ordered filed and made a part of the record in this case, all of which is now done.

And now an exception is granted by the court to each defendant to each of said conclusions of law.

And now the Court files its OPINION in this cause, which is as follows:

44 * * (Caption) * * Filed Sept 1933.

Arthur L. Gilliom, Indianapolis, Ind. attorney for plaintiff.

McMahan & Smith, Gary, Ind., attorneys for defendants.

Slick, Judge.

The facts in this case are all stipulated and the stipulation of facts is incorporated verbatim in the special findings of fact. The facts are voluminous and it is not necessary to recite in this memorandum of opinion all of the facts.

Briefly, the facts are that Commercial Trust Company of Gary drew its check on the Gary State Bank payable to the plaintiff herein in the sum of $2,196.89. This check came to the plaintiff and was deposited with Securities Trust Company of Indianapolis for collection. The Securities Trust Company in turn deposited the check with the Fletcher American National Bank of Indianapolis for collection. The Fletcher American National Bank sent the check to the National Bank of America of Gary for collection. The check

was received by the National Bank of America at Gary on December 31, 1931.

45 It was at this time, and had been for a long time, the practice and custom of the National Bank of America, when it received collections from Fletcher American National Bank, to make such collections through the clearing house at Gary and to remit by draft on Chicago. This custom was well known by Fletcher American National Bank and was followed in this case, the check being presented on December 31, 1931, to the Gary State Bank through said clearing house at Gary.

The National Bank of America closed its doors January 2, 1932. A draft of which the check in question was a part, was issued by the National Bank of America to Fletcher American National Bank, but failed to clear before the National Bank of America closed its doors. Defendant Jennings, receiver of National Bank of America, took possession of all the assets of the National Bank of America, and took possession of the $2,196.89 in question.

The question to determine in this case is whether plaintiff be allowed a preferred claim in the full amount of $2,196.89, or whether it receive on its claim only ratable dividends paid to general creditors. The serious question for decision is whether a collection made by a national bank operating in the state of Indiana where the statute provided that the collecting bank act as agent or sub-agent for the purpose of collection, shall be paid in full. In other words, does the Indiana Uniform Bank Collection Code govern here or is it a nullity so far as national banks operating in Indiana are concerned?

The federal statutes and decisions in reference to distribution of assets of insolvent national banks control and provide for ratable dividends by the Comptroller of money of a bank turned over to him by the receiver of such national bank. In other words, the receiver reduces the

46 assets to cash and turns this cash, together with all other cash belonging to the bank, over to the Comptroller, who in turn ratably divides it amongst all claimants.

The question then resolves itself to the inquiry as to whether the *money* in the hands of the receiver *collected* under the Indiana Uniform Bank Collection Code, was the *money* of the bank, and so constituted assets, or was the *money* held in, or impressed with, a trust and hence not assets of the bank, which the receiver in charge could legally

turn over to the Comptroller for ratable distribution under the federal statute.

There is no donbt that the National Banking Act and decisions of the federal courts control in the distribution of the assets of an insolvent national bank. They, the assets, must be ratably distributed to all the creditors, but did the *money* in controversy constitute assets of the bank? Did the *money* so collected belong to the bank? Did the bank get title to the *money,* or was it the *money* of plaintiff held in trust by the insolvent bank?

Defendant argues that to adopt the theory that the statute of Indiana is controlling on the question of agency is equivalent to holding that each state in the union may adopt rules for distribution of assets of insolvent national banks. The results are not so far reaching.

The federal rule is that a receiver of an insolvent national bank shall turn over for distribution the assets of the failed bank, not the assets, cash, or property of some other person held by such insolvent bank as agent or in trust. The federal rule does not require that *money* in the possession of an insolvent national bank as agent shall be considered assets.

The Indiana state rule is that *money* collected as
47 this *money* was, shall be held by the collecting bank as agent. There appears to be no conflict between the federal statute providing for ratable distribution of assets and the decisions of the federal courts under that statute and the Uniform Bank Collection Code of Indiana. National banks are amenable to the laws of the state in which they operate. They are governed in all respects by the state law except where the state law contravenes the federal law, in which case the federal law is controlling. See *McClellan* v. *Chipman,* 164 U. S. 347, where the Supreme Court of the United States lays down the rule in the following language:

> "The rule being the operation of general state laws upon the dealings and contracts of national banks, the exception being the cessation of the operation of such laws whenever they expressly conflict with the laws of the United States or frustrate the purpose for which the national banks were created, or impair their efficiency to discharge the duties imposed upon them by the law of the United States.

The court in this opinion used the following language:

> "The purpose and object of Congress in enacting the national bank law was to leave such banks as to their contracts in general under the operation of the state law,

s
3.

and thereby invest them as Federal agencies with local strength, whilst, at the same time, preserving them from undue state interference wherever Congress within the limits of its constitutional authority has expressly so directed, or wherever such state interference frustrates the lawful purpose of Congress or impairs the efficiency of
48 the banks to discharge the duties imposed upon them by the law of the United States."

The state law of Indiana provides explicitedly that the funds in question shall be held as agent or sub-agent. The federal law contains no contrary provision. To sustain plaintiff's contention is to give effect to the Indiana code as well as to the federal acts. To sustain defendant's contention would be to destroy the effect of the Indiana code as applied to national banks. The constitutionality of the Indiana Uniform Bank Collection Code is not challenged. It is and was in full force and effect at the time of this transaction.

Section 2, Chapter 164 of the Indiana Acts of 1929, page 515, provides that "where an item is deposited or received for collection, the bank of deposit shall be agent of the depositor for its collection and each subsequent collecting bank shall be sub-agent of the depositor."

Section 1 of the same act at 514, provides, that "the term 'bank' shall include any person, firm or corporation engaged in the business of receiving and paying deposits of money within this state."

No authority has been cited and, I think none can be, that directs or permits the appropriation by a receiver of funds held in trust or as agent for another person. These funds must be paid over by the receiver to the owner thereof. They do not constitute assets of the failed bank, do not belong to the bank, and the receiver has no right to hold them or pay them over to the Comptroller for distribution, or to do anything with them except to turn them over to the rightful owner, the plaintiff in this case.

THOS. W. SLICK
Judge, U. S. District Court.

September 13, 1933.

ed Sept.
1933.

49 And now the Court renders judgment and decree upon said special findings of fact and conclusions of law.

It Is Therefore Considered, Adjudged and Decreed by the Court that plaintiff have and recover of and from the defendants the total sum of $2,429.32, consisting of the principal

sum of $2,196.89 and of interest in the sum of $232.43 out of cash and cash items in the possession of the defendant David H. Jennings, as receiver of defendant National Bank of America in preference over creditors of said bank. Said defendant David H. Jennings, as such receiver, is hereby ordered to pay forthwith to plaintiff said sum of $2,429.32 in full out of cash and cash items in his possession as such receiver, and each of the defendants are hereby permanently enjoined from using so much of the cash and cash items in said receiver's possession as is needed to satisfy this judgment and decree for any purpose other than for the satisfaction of this judgment and decree.

It is further ordered that the plaintiff recover from the defendants its costs herein expended, the same to be taxed by the clerk of this Court, and have execution therefor.

(Signed) THOS. W. SLICK,
Judge.

50 And afterward, to-wit, at the November Term, 1933, of said court and on the 8th day of November, 1933, before the Honorable Thomas W. Slick, Judge of said court, the following further proceedings were had, to-wit:

Come now the defendants and file their petition for appeal, which petition reads in the words and figures, to-wit:

51 * * (Caption) * *

Filed No
1933.

PETITION FOR APPEAL.

Filed November 8, A. D. 1933.

To: The Honorable District Court of Indiana, Northern District, Hammond Division, Thomas W. Slick, Judge:

The defendants, National Bank of America, a corporation, and David H. Jennings, as Receiver for the National Bank of America, considering themselves aggrieved by the decree entered herein on the 13th day of September, 1933, in the above entitled cause, do hereby jointly and severally appeal therefrom to the Circuit Court of Appeals for the Seventh Circuit for the reasons specified in the assignment of errors, which is filed herewith, and they pray that their appeal may be allowed; that a citation be issued as provided by law, and that a transcript of the record, proceedings and papers upon

which said decree was based, be duly authenticated and sent to the Circuit Court of Appeals for the Seventh Circuit, sitting in the City of Chicago, Cook County, Illinois.

And inasmuch as this is an appeal by the Receiver of a National Bank appointed by and acting under authority
52 of the Comptroller of the Currency, your petitioners further pray that the proper order relating to the security to be required of them to perfect their appeal be made.

NATIONAL BANK OF AMERICA and
DAVID H. JENNINGS, as Receiver for the National Bank of America,
By McMAHAN, STROM & HULBERT,
Their Attorneys.

The petition granted and appeal allowed and shall act as a supersedeas without bond.

THOS. SLICK,
Judge, District Court, Northern District of Indiana.

53 And thereupon, the following further proceedings were had in said cause, to-wit:

Nov. 8. * * (Caption) * *

NOTICE BY DEFENDANTS, NATIONAL BANK OF AMERICA, AND DAVID H. JENNINGS, AS RECEIVER FOR THE NATIONAL BANK OF AMERICA, OF THE TAKING OF AN APPEAL.

To: United States Fidelity & Guaranty Company, a corporation:

You will please take notice that on the 8th day of November, 1933, at four o'clock P. M., or as soon thereafter as counsel may be heard, the defendants, National Bank of America and David H. Jennings, as Receiver for the National Bank of America, by McMahan, Strom & Hulbert, their attorneys, will apply to the Honorable Thomas W. Slick, Judge of said Court, in the room usually occupied by him as a courtroom, at 507 State Street, Hammond, Indiana, District and Division aforesaid, for the allowance of an appeal from the decree of said United States District Court

entered on the 13th day of September, 1933, in the above entitled cause.

NATIONAL BANK OF AMERICA and
DAVID H. JENNINGS, as Receiver for
National Bank of America.
By McMAHAN, STROM & HULBERT,
Their Attorneys.

We hereby acknowledge service of the foregoing notice and receipt of a copy thereof this 4th day of November, 1933.

ARTHUR L. GILLIOM,
Attorney for the Plaintiff, United States Fidelity & Guaranty Company, a corporation.

Filed Nov. 8, 1933. Margaret Cowgill, Clerk.

54 And thereupon the following further proceedings were had in said cause, to-wit:

Come now the defendants and file their assignment of errors, which reads in the words and figures following, to-wit:

55 * * (Caption) * * Filed Nov. 1933.

ASSIGNMENT OF ERRORS.

Come now the defendants, National Bank of America, a corporation, and David H. Jennings, as Receiver for the National Bank of America, by McMahan, Strom & Hulbert, their counsel, and jointly and severally respectfully represent and say to this Honorable Court that the decree entered in the above cause on the 13th day of September, 1933, A. D., is erroneous and unjust to the defendants. And said defendants file and submit the following assignment of errors upon which they and each of them will rely upon their appeal from said decree, and say that this Honorable Court erred in the following respects:

First: The Court erred in each of its several conclusions of law numbered One, Two, Three and Four.

Second: The Court erred in holding and decreeing that the plaintiff have and recover of and from the defendants the sum of $2,429.32, consisting of the principal sum of $2,196.89 and of interest in the sum of $232.43 out of the cash and cash items in the possession of the defendant, David

H. Jennings as Receiver for the National Bank of America, in preference over other creditors of said bank.

Third: The Court erred in holding and decreeing
56 that the plaintiff have and recover from the defendants the sum of $232.43 as interest on the sum of $2,196.89 adjudged and decreed to be owing the plaintiff.

Fourth: The Court erred in holding and decreeing that the sum of $2,429.32, or any part thereof, was a preferred claim to be paid by the Receiver in preference over creditors of the National Bank of America.

Fifth: The Court erred in enjoining each of the defendants from using so much of the cash and cash items in the possession of the defendant, David H. Jennings, as Receiver for the National Bank of America as needed to satisfy the judgment and decree appealed from.

Sixth: The Court erred in ordering and decreeing that the plaintiff recover from the defendants its costs, and that it should have execution therefor.

Seventh: The Court erred in not adjudging and decreeing that the plaintiff was entitled to recover of and from the defendants the sum of $2,196.89 and no more, as a general claim, to be paid by the Receiver of the National Bank of America out of the assets of said bank in the due course of the liquidation of said bank.

Eighth: The Court erred in decreeing that the cash items of the defendant, National Bank of America, became impressed with a trust in the plaintiff's favor in the sum of $2,196.89, and that the defendant, David H. Jennings, as Receiver for the National Bank of America, took over and received said sum of money subject to such trust.

Ninth: The facts found by the Court do not warrant or sustain the decree of the Court, that the plaintiff is entitled to have its claim allowed and paid out of the assets of the
57 National Bank of America in the possession of the Receiver, as a preferred claim.

Tenth: The Court erred in holding the preferred claim provisions of the Indiana Law, Chapter 164, Acts 1929, page 514, applies in winding up the affairs of a National Bank which is being liquidated under the National Bank Act.

Eleventh: The Court erred in holding that the provisions of the Act of the General Assembly of the State of Indiana, entitled: "An Act to expedite and simplify the collection and payment by banks of checks and other instruments for the payment of money," approved March 13, 1929, Acts 1929, page 514, is applicable in winding up the affairs of an insolvent National Bank which is being liquidated by a re-

ceiver appointed by the Comptroller of the Currency, and under the provisions of the National Bank Act.

Wherefore, the defendants jointly and severally pray that the said decree be reversed and that the District Court be instructed to enter a decree adjudging and decreeing that there is due and owing the plaintiff the sum of $2,196.89 as a general claim against the National Bank of America, to be paid in the course of administration, or that the Court of Appeals reverse said decree and render a decree on the record in favor of plaintiff for the sum of $2,196.89 as a general claim.

McMAHAN, STROM & HULBERT,
Attorneys for Defendants.

58 And thereupon, the following further proceedings were had in said cause, to-wit:

Come now the parties and file their stipulation waiving bond on appeal, which stipulation reads in the words and figures following, to-wit:

59 * * (Caption) * * Filed Nov. 1933.

STIPULATION WAIVING BOND ON APPEAL.

It is hereby stipulated by and between the parties hereto that with the approval of the court the filing of a bond by the appellants, National Bank of America and David H. Jennings, Receiver for the National Bank of America, on appeal from the decree or order of this court dated September 13, 1933, is hereby waived, and that such appeal may be prosecuted without the filing of such bond.

Dated November 8, 1933.

ARTHUR L. GILLIOM,
Attorney for Plaintiff.
McMAHAN, STROM & HULBERT,
Attorneys for Defendants.

66 And afterwards, to-wit, at the November Term of said court, and on the 5th day of December, 1933, before the Honorable Thomas W. Slick, Judge of said court, the following further proceedings were had in said cause, to-wit:

Come now the defendants and file petition for extension of time for filing transcript in Circuit Court of Appeals, which petition reads in the words and figures following, to-wit:

67 * * (Caption) * *

PETITION FOR EXTENSION OF TIME FOR FILING TRANSCRIPT IN CIRCUIT COURT OF APPEALS.

Comes now the defendants, National Bank of America and David H. Jennings, Receiver of National Bank of America, and shows to the court that heretofore, to-wit, on November 8, 1933, the said defendants filed their petitions herein for an appeal from the decree theretofore entered herein, to United States Circuit Court of Appeals of the Seventh Circuit; that said appeal was on said last named day, granted, and said defendants time for filing their transcript and perfecting appeal expires December 8, 1933; that citation was served upon the plaintiff on the 10th day of November, 1933, and that on the 13th day of November, 1933, these defendants filed their praecipe for a transcript of the record in the office of the clerk of this court; that the clerk of this court, because of the great volume of work which the clerk has been required to do since the 13th day of November, 1933, she has been unable to, and will not be able to prepare said transcript in time for the defendant's to file the same on or before December 8, 1933;

68 Wherefore, the defendants ask that the time within which they shall file their transcript in the office of the Clerk of the Circuit Court of Appeals be extended and enlarged to and including the 22nd day of December, 1933.

WILLIS C. MCMAHAN,
Attorney for Defendants.

State of Indiana, } ss:
County of Lake. }

WILLIS. C. McMAHAN, being duly sworn, deposes and says, that he is one of the attorneys for the defendants in the above entitled cause; that he has authority to and does make this affidavit for and on behalf of said defendants and states that the facts set forth in the above and foregoing petition are true. Further the affiant saith not.

WILLIS C. MCMAHAN.

Subscribed and sworn to before me this 5th day of December, 1933.

FRANK L. GREENWALD,
Notary Public.

My Commission Expires: 9/14/37

69 And thereupon, the following further proceedings were had in said cause, to-wit:

70 * * (Caption) * *

ORDER ON PETITION FOR EXTENSION OF TIME FOR FILING TRANSCRIPT IN CIRCUIT COURT OF APPEALS.

Comes now the defendants, National Bank of America, and David H. Jennings, as Receiver for the National Bank of America, and files their petition in these words insert: for an enlargement of time in which to file the transcript and record in the clerk's office of the United States Circuit Court of Appeals, Seventh Circuit, and the court having examined the same now grants said petition and gives unto the said defendant to and including the 22nd day of December, 1933, within which to file said record and transcript with the clerk of said Circuit Court of Appeals; all of which is adjudged this 5th day of December, 1933.

THOS W. SLICK,
Judge.

63 And afterward, to-wit, on the 13th day of November, 1933, being the November Term of said court, before the Honorable Thomas W. Slick, Judge of said Court, the following further proceedings were had, to-wit: Filed Nov. 1933.

Come now the defendants and file their praecipe for record, which praecipe reads as follows, to-wit:

64 * * (Caption) * *

PRAECIPE FOR RECORD.

To: The Clerk of the Above Court:

You are hereby requested to make a transcript of the record in the above captioned cause to be filed in the United States Circuit Court of Appeals for the Seventh Circuit, pursuant to an appeal allowed in the above entitled cause, and to include in such transcript of record the following, and no other papers and exhibits, to-wit:

1. The complaint.
2. The petition to remove from the Lake Circuit Court of

Indiana to the United States District Court for the Northern District of Indiana.

3. The notice of the filing of petition to remove and the acknowledgement of service of such notice.
4. Bond for Removal.
5. Stipulation to transfer to South Bend Division.
6. The answer filed May 15, 1933.
7. Plaintiff's Exhibit 1, being the agreed statement of facts.
8. Finding of Facts and Conclusions of Law.
9. Opinion of the Court.
10. The decree of the Court.

65 11. Notice of intention to apply for order allowing an appeal and acknowledgment of service of same.

12. Petition for allowance of appeal and endorsement of Judge allowing appeal.
13. Assignment of Errors.
14. Stipulation waiving bond on appeal.
15. Citation and acknowledgement of service.
16. This praecipe.
17. Clerk's certificate.

Said transcript to include all record entries and orders entered in said cause and to be prepared as required by law and the rules of this court and the rules of the United States Circuit Court of Appeals for the Seventh Circuit and to be filed in the office of the Clerk of the Circuit Court of Appeals for the Seventh Circuit, on or before the 8th day of December, 1933.

In copying the order showing the filing of the stipulation of facts, you will not copy such stipulation in such order, but you will, at the proper place in such order, refer to the special finding of facts where such stipulation is set out in full and indicate that a copy of such stipulation is set out in full in the special finding of facts.

McMahan, Strom & Hulbert,
Attorneys for Appellants, National Bank of America and David H. Jennings, Receiver for National Bank of America.

Dated this 8th day of November, 1933.

Service of the above praecipe accepted and acknowledged this 8th day of November, 1933.

Arthur L. Gilliom,
Attorney for Appellee, United States Fidelity & Guaranty Company, a corp.

71 IN THE DISTRICT COURT OF THE UNITED STATES

For the Northern District of Indiana,

Hammond Division.

CERTIFICATE OF THE CLERK OF THE DISTRICT COURT OF THE UNITED STATES FOR THE NORTHERN DISTRICT OF INDIANA.

I, Margaret Cowgill, Clerk U. S. District Court, of the Northern District of Indiana, do hereby certify the above and foregoing to be a true and complete transcript of proceedings had of record, prepared and made by me as required by the praecipe filed in the cause entitled United States Fidelity & Guaranty Company, a corporation, *vs.* National Bank of America and David H. Jennings, as Receiver for the National Bank of America, as the same appear from the original records and files thereof now remaining in my custody and control.

In Testimony Whereof, I have hereunto set my hand and affixed the seal of said court at my office in the City of Hammond, in said District, this 21st day December, 1933.

MARGARET COWGILL,
Clerk.

(Seal)

By BEULAH MCCABE,
Deputy.

60 And thereupon, the following further proceedings were had in said cause, to-wit:

And now a citation is ordered, which citation reads as follows, to-wit:

61 * * (Caption) * *

CITATION.

The United States of America to United States Fidelity & Guaranty Company, a corporation:

You are hereby cited and admonished to be and appear in the United States Circuit Court of Appeals for the Seventh Circuit to be holden in the City of Chicago, Cook county, Illinois, within thirty (30) days from the date hereof, pursuant to a petition for appeal filed in the Clerk's office of the District Court of the United States for the Northern District of Indiana, Hammond Division, wherein the United States Fidelity and Guaranty Company is the plaintiff and the National Bank of America and David H. Jennings, as Receiver of the National Bank of America are defendants, to show cause, if any there be, why the decree in said petition for appeal mentioned should not be corrected and speedy justice be done in that behalf.

Given under my hand at the City of Hammond in the District and Circuit aforesaid, this, the 8 day of November, 1933, A. D.

THOS. W. SLICK,
United States District Judge for the Northern District of Indiana, Hammond Division.

Service of a copy of the above citation is hereby acknowledged this 10th day of November, 1933.

PICKENS, DAVIDSON, GAUSE, GILLIOM & PICKENS,
ARTHUR L. GILLIOM,
Attorneys for Plaintiff.

62 (Endorsed) * * (Caption) * * Citation Filed Nov 13 1933 Margaret Cowgill, Clerk. U. S. District Court.

UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

I, Frederick G. Campbell, Clerk of the United States Circuit Court of Appeals for the Seventh Circuit, do hereby certify that the foregoing printed pages numbered from 1 to 40, inclusive, contain a true copy of the printed record, printed under my supervision and filed on the eighteenth day of January, 1934, and used and considered at the hearing and on the determination of the following entitled cause:

National Bank of America and David H. Jennings, as Receiver of the National Bank of America,
Appellants,

vs.

United States Fidelity and Guaranty Company,
Appellee,

No. 5124, October Term, 1933, as the same remains upon the files and records of the United States Circuit Court of Appeals for the Seventh Circuit.

In Testimony Whereof I hereunto subscribe my name and affix the seal of said United States Circuit Court of Appeals for the Seventh Circuit, at the City of Chicago, this 22nd day of June, A. D. 1934.

FREDERICK G. CAMPBELL,
Clerk of the United States Circuit Court of Appeals for the Seventh Circuit.

(Seal)

At a regular term of the United States Circuit Court of Appeals for the Seventh Circuit, begun and held in the United States Court Room, in the City of Chicago, in said Seventh Circuit, on the third day of October, 1933, of the October Term, in the year of our Lord One Thousand Nine Hundred and Thirty-Three, and of our Independence the One Hundred and Fifty-Eighth.

National Bank of America and David H. Jennings, as Receiver,
5124 *vs.*
United States Fidelity & Guaranty Company.

Appeal from the District Court of the United States for the Northern District of Indiana, Hammond Division.

And on, to-wit: On the twenty-second day of December, 1933, there was filed in the office of the Clerk of this court an appearance of counsel for appellants, which said appearance is in the words and figures following, to-wit:

UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5124. October Term, 1933.

National Bank of America and David H. Jennings, as Receiver,
Appellants,

vs.

United States Fidelity and Guaranty Company, a Corporation,
Appellee.

The Clerk will enter my appearance as counsel for the appellants.

WILLIS C. MCMAHAN,
569 Broadway,
Gary, Indiana.

Endorsed: Filed January 18, 1934, Frederick G. Campbell, Clerk.

And afterwards, to-wit: On the twenty-sixth day of December, 1933, there was filed in the office of the Clerk of this court the appearance of counsel for appellee, which said appearance is in the following words and figures, to-wit:

UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5124. October Term, 1933.

National Bank of America and David H. Jennings, as Receiver,

Appellants,

vs.

United States Fidelity and Guaranty Company, a Corporation,

Appellee.

The Clerk will enter my appearance as counsel for the appellee.

ARTHUR L. GILLIOM,
Fletcher Trust Building,
Indianapolis, Indiana.

Endorsed: Filed December twenty-sixth, 1933, Frederick G. Campbell, Clerk.

And afterwards, to-wit: On the tenth day of April, 1934, the following further proceedings were had and entered of record, to-wit:

Tuesday, April 10, 1934.

Court met pursuant to adjournment and was opened by preclamation.

Before:

Hon. Samuel Alschuler, Circuit Judge.
Hon. Evan A. Evans, Circuit Judge.
Hon. William M. Sparks, Circuit Judge.

5124 National Bank of America, *et al.*, *vs.* United States Fidelity & Guaranty Company. } Appeal from the District Court of the United States for the Northern District of Indiana, Hammond Division.

It is ordered by the court that this cause be, and the same is hereby set down for hearing on April 13, 1934.

And afterwards, to-wit: On the thirteenth day of April, 1934, the following further proceedings were had and entered of record, to-wit:

Friday, April 13, 1934.

Court met pursuant to adjournment and was opened by proclamation.

Before:

Hon. Evan A. Evans, Circuit Judge.
Hon. William M. Sparks, Circuit Judge.
Hon. Louis FitzHenry, Circuit Judge.

5124 National Bank of America, *et al.* *vs.* United States Fidelity and Guaranty Company. } Appeal from the District Court of the United States for the Northern District of Indiana, Hammond Division.

Now this day come the parties by their counsel and this cause now comes on to be heard on the printed record and briefs of counsel and on oral arguments by Mr. Willis C. McMahan, counsel for appellants, and by Mr. Arthur C. Gilliom, counsel for appellee, and the court having heard the same takes this matter under advisement.

And afterwards, to-wit: On the fourth day of June, 1934, there was filed in the office of the Clerk of this court the opinion of the court, which said opinion is in the words and figures following, to-wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5124. October Term, 1933, April Session, 1934.

NATIONAL BANK OF AMERICA and DAVID H. JENNINGS, as Receiver of the National Bank of America, *Appellants*,

v.

UNITED STATES FIDELITY AND GUARANTY COMPANY, *Appellee.*

Appeal from the District Court of the United States for the Northern District of Indiana, Hammond Division.

June 4, 1934.

Before EVANS, SPARKS, and FITZHENRY, *Circuit Judges.*

SPARKS, *Circuit Judge.* Appellee instituted this action in equity against the National Bank of America of Gary, Indiana, and David H. Jennings, its receiver, to recover the amount of a check which had been drawn on the Gary State Bank and mailed to and collected by the National Bank of America through the Gary Clearing House before the National Bank had closed.

On December 30, 1931, appellee received from the Commercial Trust Company of Gary that company's check for $2196.89, dated December 29, 1931, and payable to the order of appellee. On the date of its receipt appellee endorsed and deposited it with the Security Trust Company of Indianapolis, which in turn endorsed and delivered it to the Fletcher American National Bank of Indianapolis. That bank also endorsed and mailed it to its correspondent, the appellant bank,

for collection and remittance. The last named bank received it on the morning of December 31, 1931, and on the same day presented and collected it in the manner hereinafter described, from the Gary State Bank through the Gary Clearing House, whose membership consisted solely of the Gary banks hereinbefore mentioned.

In addition to this check, appellant bank had received other checks drawn on the Gary State Bank and the First National Bank of Gary, and as a result of the clearings of that day, appellant bank owed the clearing house $1044.75, for which sum it drew its check on the Continental Illinois Bank and Trust Company of Chicago, payable to the order of the clearing house. As a result of the clearing house transaction the Gary State Bank received the check for $2196.89, stamped it paid, charged it to the account of the Commercial Trust Company, and delivered it to the drawer.

All the banks herein referred to were closed for holiday on January 1, 1932, and on Sunday, January 3, the directors of appellant bank met and adopted a resolution not to open for business on January 4, at which time the bank was insolvent. The Comptroller of the Currency was notified, and the receiver took charge of the assets at eight o'clock on the morning of January 4.

On and prior to January 2, 1932, it was the custom of the Fletcher Bank to send checks drawn on Gary banks to appellant bank for collection, and the custom of the latter to present those checks to the Gary Clearing House for collection, and when collected, appellant bank would mail its check or draft on its correspondent bank to the Fletcher Bank in payment of the collection so made. That custom was followed in this instance.

The total amount of checks sent by the Fletcher Bank to and received by appellant bank on December 31, was $3660.83, and they were collected on that date through the clearing house, and appellant bank drew its draft on the Continental Bank for that amount and sent it to the Fletcher Bank, which in turn mailed it the same day to the Continental Bank, by which it was received on January 4, after appellant bank was closed. Hence payment was refused. At that time appellant bank had on deposit with the Continental a sum in excess of the amount of the draft.

The Fletcher Bank received the unpaid draft from the Continental on January 5, 1932, and charged it to the account of appellant bank, which left a deposit balance due appellant

bank from the Fletcher Bank of $333.91, which was paid to the receiver on March 3, 1932. Subsequently upon demand the Fletcher Bank paid to the receiver the amount of the draft which it had charged to appellant bank, and thereupon charged the amount of the check for $2196.89 against the Security Trust Company, which in turn charged the same amount to appellee's account. At the time the receiver took charge of appellant bank there were, and ever since that time there have been, in its possession, cash items in excess of appellee's claim.

The court found the facts specially and rendered its conclusions of law, and entered a decree for appellee for the full amount of the check, with interest, as a preferred claim. The theory upon which the bill and the decree were based was that at the time of the bank's insolvency it held in trust the amount of the proceeds of appellee's check among its cash and cash items, and that those proceeds constituted no part of the bank's assets, hence were not distributable to its creditors.

Whether a trust relationship existed between the bank and appellee, by virtue of the circumstances hereinbefore set forth, is to be determined by sections 1, 2, 9, and 10 of the Indiana Uniform Bank Collection Code, ch. 164, Indiana Acts, 1929. Section 1 defines the word "bank" as meaning any person, firm or corporation engaged in the business of receiving and paying deposits of money, and the word "item" as meaning any check, note or other instrument for the payment of money. Section 2 provides that, unless otherwise agreed, a bank receiving an item on deposit for collection, and all subsequent banks receiving it for that purpose, are agents and subagents, respectively, of the depositor. Section 9 provides that where ordinary care is exercised, any agent collecting bank, without becoming responsible as debtor therefor, may receive in payment of an item, whether presented by mail, through the clearing house, or over the counter of the drawee or payor, in lieu of money, either the check or draft of the drawee or payor upon another bank, or check or draft of any other bank upon any bank other than the drawee or payor of the item, or it may make such settlement as may be customary in a local clearing house or between clearing banks or otherwise. A proviso of this section states that the agent collecting bank shall become liable as debtor for the item as if it had actually received payment in cash, if at the time of receipt it shall request or accept in payment an unconditional

credit which has been given to it on the books of the drawee or payor, or on the books of any other bank. Section 10 provides that any agent collecting bank, in lieu of money, may receive from any subsequent bank in the chain of collection, remittance for an item which has been paid, in the same manner as set forth in section 9, and with the same provision with respect to establishing a debtor relationship upon the request or acceptance of an unconditional credit. In view of those sections of the Indiana Code it is obvious that the relationship existing between appellant bank and appellee, from and subsequent to the time it received the check for collection was that of agent and principal, and not mere debtor and creditor.

In the absence of statutory authority, or authority expressly granted by the terms of the agency, the collecting bank had no right to accept anything in payment except legal tender money, and if it had done so, the relationship of debtor and creditor would have arisen because the collecting bank in accepting other than cash in payment of the check would not have been acting within the scope of its agency (*Federal Reserve Bank* v. *Malloy,* 264 U. S. 160) and the trust relationship would not follow a subsequent transfer of the thing received as payment. But the first clause of section 9 specifically authorized the bank to receive the exchanged checks drawn on it and presented to it through the clearing house, in lieu of money in payment of appellee's check, without becoming responsible as debtor. It is true that the proviso in section 9 supplies means for establishing a debtor relation, but those means are not present here. It must be held under the state statute, therefore, that appellant was the agent of appellee, and in receiving the proceeds of the check it did so as trustee for appellee.

It is contended by appellants, however, that the Indiana statute will not override the provisions of R. S. 5236, 12 USCA sec. 194, which provides for the distribution by the Comptroller of the entire assets of the bank, giving no preference to any claim except for moneys to reimburse the United States for advances in redeeming the notes. With respect to state legislation affecting national banks, the Supreme Court said, in *McClellan* v. *Chipman,* 164 U. S. 347:

> "First. National banks 'are subject to the laws of the State, and are governed in their daily course of business far more by the laws of the State than of the nation. All their contracts are governed and construed by state laws. Their acquisition and transfer of property, their right to

collect their debts, and their liability to be sued for debts, are all based on state law. It is only when the state law incapacitates the banks from discharging their duties to the government that it becomes unconstitutional.' *National Bank* v. *Commonwealth*, 9 Wall. 362.

"Second. 'National banks are instrumentalities of the Federal government created for a public purpose, and as such necessarily subject to the paramount authority of the United States. It follows that an attempt by a State to define their duties, or control the conduct of their affairs, is absolutely void, whenever such attempted exercise of authority expressly conflicts with the laws of the United States, and either frustrates the purpose of the national legislation, or impairs the efficiencies of these agencies of the Federal government to discharge the duties for the performance of which they were created.' *Davis* v. *Elmira Savings Bank*, 161 U. S. 275."

There is nothing in the Indiana statutes that attempts to interfere with the Comptroller's distribution of the bank's assets. The proceeds of appellee's check were not rightfully a part of its assets, and there is no effort here to secure a preference over any creditor in the distribution of the assets, or to interfere with the Comptroller in that respect. The effort on the part of appellee is merely to recover its own property which under the laws of Indiana was held in trust by the bank as agent for appellee. We know of no federal pronouncement which holds that a national bank may include in its distributable assets to its general creditors a fund which is held by it as trustee, when that fund has been traced into the hands of the receiver. There has been a contrariety of opinion among the state courts as to when a trust relationship arises with respect to banks acting as collectors of commercial paper, but not as to the Comptroller's duty when once that relationship is established. The right of Indiana to establish that relationship by legislative enactment was well within its powers and is controlling here.

The mere fact that a debtor and creditor relationship did not arise, under the Indiana statute, by virtue of acceptance and receipt by the appellant bank of some medium other than cash in payment for appellee's check, is not sufficient, however, to support a finding for appellee, unless it be shown that as a result of the transaction there was an augmentation of the cash and cash items of appellant bank; and that the proceeds of the collection have been traced into the hands of the receiver.

It is contended by appellants that the assets of the insolvent bank were not augmented by the transaction, for the reason that it received no actual money on account of the collection item, but used the check which it had received from the drawee, Gary State Bank, to pay items drawn on itself in the clearings. The cases cited to this proposition unquestionably support it, but it is contended by appellee that in none of those cases was the Uniform Bank Collection Code involved; that there the court held that the collecting bank had violated its agency agreement by wrongfully accepting payment in other than cash, which had the effect of raising a debtor and creditor relationship, whereas the Indiana enactment authorized the character of the payment and preserved the relationship of principal and agent.

It is quite obvious that that result was one of the principal objects of the Uniform Bank Collection Act, and we are convinced that its involvement here is quite sufficient to distinguish the instant case from those relied upon by appellants.

Appellee argues that when appellant bank exchanged appellee's check on the Gary State Bank for checks which the latter held against the former at the clearing house transaction, appellee's check, by virtue of section 9 of the Indiana Act, was not used to pay the appellant's debt to the clearing house, but it was a collection of the check in a manner authorized by the Act; hence that which it received is to be considered as proceeds of the check, and since appellant bank did not request or accept an unconditional credit for the item on the books of the Gary State Bank, or of any other bank, as provided under section 9, the bank did not become responsible as debtor for either the check or its proceeds, but it still was liable as agent. It further contends that the proceeds thus received in payment were the same as cash to appellant bank and were in contemplation of section 9 automatically reflected in the cash and cash items of that bank, after the clearing house transaction, because the cash and cash items became instantly relieved from the obligations of the checks received in exchange to the extent of appellee's check, and that the legal effect of the transaction was a substitution of cash and cash items held by appellant bank to the extent of $2196.89 for checks upon itself which it received as agent in payment of appellee's check. Hence it says there was augmentation of the cash and cash items to the extent of the proceeds of appellee's check, toward which appellant bank remained a fiduciary.

We are in accord with appellee's contention in this respect. It is conceded by appellants that if the balance of the clearings had been in favor of appellant bank it would be presumed that such balance was the proceeds of the collection item and should be allowed as a preferred claim, providing said balance had been paid in cash, and had been traced into the hands of the receiver. It must also be conceded that if appellant bank had paid cash to the clearing house for said bank's outstanding checks, and the clearing house had in turn delivered the cash to the bank in payment of appellee's check, and the proceeds had been traced into the hands of the receiver, those proceeds would be considered as held in trust by the bank for appellee by reason of the relationship of principal and agent. Under those circumstances augmentation of assets would clearly appear, notwithstanding the fact that the bank's assets were the same in amount as they were before the clearings, because during such process of clearing the assets would have been reduced by the cash payment to the clearing house and augmented in the same amount by the cash payment of the clearing house to the bank. Under the Indiana statute, however, it was immaterial whether actual cash passed in the transaction, for the result is identical, and the relationship of debtor and creditor did not arise. Appellant bank held the proceeds of appellee's check in a fiduciary capacity and it was its duty to treat them as such. This it did by immediately retaining and cancelling its own checks received from the clearing house, and drawing its draft on its cash balance in the Continental and sending it to the forwarding bank at Indianapolis. In other words, instead of taking the cash from its vaults and paying its indebtedness at the clearing house and in turn receiving it from the clearing house in payment of appellee's check, which in theory it was its duty to do, appellant bank obviously considered these things as having been done. To hold otherwise would be to presume that it had applied the proceeds of appellee's check to the payment of its own indebtedness thereby violating its trust relationship. The law will not presume that this was done, but rather that it regarded its trust obligation and kept it sacred. *Brennan* v. *Tillinghast*, 201 Fed. 609. We think it clear that the legal effect of the transaction was a substitution of cash and cash items held by appellant bank to the extent of $2196.89 in amount, for checks upon it which it received as agent in payment of appellee's check. It is stipulated that, but for the collection of appellee's check, appellant

bank would that day have actually paid to the clearing house the sum of $2196.89 more than it did pay, and the assets for distribution to creditors would have been decreased by that amount. In *Ellerbe* v. *Studebaker Corporation of America,* 21 F. (2d) 993, the court said, " * * * there can be no doubt that, as a result of the collection of the draft of complainant, the assets which came into the hands of the receiver were greater by the amount of the collection than they would have been had the collection not been made, and consequently that there was that much more for division among creditors than there would have been otherwise."

If appellee's check is to be considered as having been paid by the exchange of the unpaid checks of appellant bank, then it is clear that appellee would have been entitled to the bank's checks which were delivered to it by the clearing house, for under those circumstances appellee would have been subrogated to the rights of the original payees of the bank's checks. But it is obvious that the bank did not consider that appellee's check had in fact paid the bank's checks, for it retained and cancelled them, and this it could not rightfully do unless a corresponding amount of cash on hand be considered as substituted, on behalf of appellee, for the unpaid checks received from the clearing house. If appellants' contention be sustained they are placed in the situation of having received and retained the full amount of appellee's check, and also the bank's own checks for which it or the receiver paid nothing. It cannot be denied that appellee's check was paid by the Gary State Bank, and its assets were reduced by that amount, and it is equally clear that the same amount came into the possession of appellant bank. The clearing house transaction was practically instantaneous, yet it consisted of two distinct acts, the collection of appellant bank's obligations, and the payment of appellee's check. If either be considered as happening before the other, then it is clear that appellant bank's assets were augmented by the proceeds of appellee's check, and they were depleted by the payment of the bank's outstanding checks, and as a result the assets aggregated the same as before the clearance. As between the clearing house and appellant bank the latter's checks as a matter of commercial convenience were considered rightfully paid under the Indiana law, but as between the bank and appellee they were not paid by the bank, unless it be considered that a corresponding amount of cash was substituted for the unpaid checks. To

hold that there was no substitution would be presuming that the bank was guilty of wrong doing which is utterly inconsistent with its actions, and permit the creditors to participate in augmented assets to which they are not entitled, as a result of the wrongdoing. To hold otherwise would be consistent with the bank's actions and establish its good faith in performing the obligations of the trust. We hold, therefore, that the bank's assets were augmented by the receipt of the proceeds of appellee's check, and that those proceeds went into and were intermingled with the cash balance of the bank which was received by the receiver. Since the amount in the hands of the receiver was never reduced below the amount of the check, it follows that appellee is entitled to recover an amount equal to the face of the check. *Schumacher* v. *Harriett*, 52 F. (2d) 817.

We are convinced, however, that appellee is not entitled to recover interest. *White* v. *Knox*, 111 U. S. 784; *Richardson* v. *Louisville Banking Company*, 94 Fed. 442; *Hallett* v. *Fish*, 123 Fed. 201.

That part of the judgment which allows interest is reversed, and in all other respects the judgment is affirmed. The cause is remanded with instructions to modify the judgment by eliminating the amount allowed for interest.

And on the same day, to-wit: On the fourth day of June, 1934, the following further proceedings were had and entered of record, to-wit:

Monday, June 4, 1934.

Court met pursuant to adjournment and was opened by proclamation.

Before:

Hon. Evan A. Evans, Circuit Judge.
Hon. William M. Sparks, Circuit Judge.
Hon. Louis FitzHenry, Circuit Judge.

National Bank of America and David H. Jennings, as Receiver of the National Bank of America,
5124 *vs.*
United States Fidelity and Guaranty Company.

Appeal from the District Court of the United States for the Northern District of Indiana, Hammond Division.

This cause came on to be heard on the transcript of record from the District Court of the United States for the Northern District of Indiana, Hammond Division, and was argued by counsel.

On consideration whereof: It is now here ordered and adjudged by this court that that part of the judgment of the said District Court in this cause which allows interest, be, and the same is hereby reversed; and in all other respects the said judgment be, and the same is hereby affirmed with costs.

It is further ordered that this cause be, and the same is hereby remanded to the said District Court with instructions to modify the judgment by eliminating the amount allowed for interest.

And afterwards, to-wit: On the nineteenth day of June, 1934, there was filed in the office of the Clerk of this court an application for stay of the mandate, which said application for stay of the mandate is in the words and figures following, to-wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

October Term, A. D., 1933.

No. 5124.

National Bank of America and David H. Jennings, as Receiver of the National Bank of America,
Appellants,

vs.

United States Fidelity & Guaranty Company,
Appellee.

APPLICATION FOR STAY OF PROCEEDINGS TO PERMIT APPLICATION FOR CERTIORARI.

Petition of National Bank of America and David H. Jennings, as Receiver for the National Bank of America, appellants above named for an order staying the execution and the enforcement of the decree of the United States Circuit Court of Appeals for the Seventh Circuit, affirming the United States District Court, Northern District of Indiana, to enable said National Bank of America and David H. Jennings, as Receiver of the National Bank of America to apply for and obtain writ of certiorari from the Supreme Court.

To the honorable William M. Sparks, Judge of the United States Circuit Court for the Seventh Circuit.

Your petitioners, National Bank of America and David H. Jennings, as Receiver for National Bank of America, respectfully present this their application for an order staying the execution and enforcement of the decree of the United States Circuit Court of Appeals for the Seventh Circuit, affirming the United States District Court, Northern District of Indiana, Hammond Division, in the above entitled cause, under the provisions of Section 350, Title 28, of the United States

Code to enable said petitioners to apply for and obtain a writ of certiorari from the Supreme Court of the United States.

The grounds upon which said petition for certiorari will be based are as follows:

1. The decision of this Honorable Court that Sections 1, 2, 9, and 10 of the Indiana Uniform Bank Collection Code, chapter 164, Indiana Acts, 1929, that the relationship existing between the National Bank of America and the United States Fidelity and Guaranty Company from and after the time said bank received the said check for collection, as mentioned and set forth in the opinion and decision of this court, was agent and principal and not debtor and creditor is in conflict with decisions of the Circuit Court of Appeals for the Fifth Circuit on the same subject matter in the case if *City of Miami* v. *First National Bank,* 69 Fed. (2nd) 346.

2. The decision of this Honorable Court by holding that the Indiana Uniform Bank Collection Code, chapter 164, Acts 1929, applied to and controlled the action of the receiver of an insolvent national bank is an erroneous decision of an important question of general law and is in conflict with the weight of authority.

3. That the decision of this Honorable Court as an augmentation of the funds of the National Bank of America by the use of the check which the United States Fidelity and Guaranty Company sent to the National Bank of America for collection, in discharging and paying the obligation of the National Bank of America to the clearing house, when the balance of the clearings of that day were against the National Bank of America, by holding and deciding that such transaction was not a use by the National Bank of America of the said check for the payment of a debt of the National Bank of America to the clearing house but "was a collection of the check in a manner authorized" by the Indiana Bank Collection Code although the balance of the clearings that day was against the National Bank of America, and that the funds and the assets of the National Bank of America was thereby augmented the same as if said bank had in making the collection of said check received the proceeds of said collection in cash, is an erroneous decision of an important federal question of law of great importance to the business world, to the legal profession, and to the Comptroller of the Currency, who is now engaged in liquidating numerous insolvent national banks, and which question has not been here-

tofore, but which should be decided by the Supreme Court so as to furnish an authoritative decision as to whether the funds of a national bank are augmented when a collection is made as the collection was made in the instant case.

4. The decision of this Honorable Court as to the augmentation of the funds of the National Bank of America by holding "that the bank's assets were augmented by the receipt of the proceeds of appellee's check, and that those proceeds went into and were commingled with the cash balance of the bank which were received by the receiver", is a decision of a federal question of law relating to the liquidation of insolvent national banks in a way, which is probably in conflict with the decisions of the Supreme Court.

5. The decision of this Honorable Court to the effect that the proceeds of the collection of the check which was collected by the National Bank of America through the clearing house were not dissipated when it was used by the National Bank of America to pay its clearing indebtedness to the clearing house, is in conflict with decisions of the Supreme Court of United States, and with the decisions of other Circuit Courts of Appeals.

6. The final disposition of this cause is of distinct class importance in the settlement of similar claims against insolvent national banks, being liquidated by the Comptroller of the Currency, and the decision of this Honorable Court is in a way probably in conflict with decisions of the United States Supreme Court applicable to the liquidation of the assets of insolvent national banks by the Comptroller of the Currency and calls for the United States Supreme Court's power of supervision.

The reasons why a stay is deemed necessary are as follows: The judgment of this Honorable Court and of the District Court as modified by the decree of this court requires that the appellant, David H. Jennings, as Receiver of the National Bank of America, pay forthwith to the appellee the sum of $2196.89 out of the cash and cash items in his possession, and permanently enjoin him as such receiver from using so much of the cash and cash items in his possession as may be necessary to satisfy said decree. Under this decree and mandate an execution can be issued to enforce and satisfy said decree and if the said receiver fails to pay and satisfy the amount decreed to be due the appellee, he will be guilty of contempt of court and subject to punishment therefor. If said receiver is compelled to pay and satisfy the said

sum so decreed to be due the appellee and the decision of this court is reversed by the United States Supreme Court further litigation may arise out of an attempt to force a return or repayment of any part of the money so paid by said receiver on account of the payment thereof to appellee.

Dated this 19th day of June, 1934.

WILLIS C. MCMAHAN,
Counsel for Petitioners.

OSCAR C. STROM,
GEORGE W. HULBERT,
Of Counsel.

Comes now the appellants, National Bank of America and David H. Jennings, as Receiver of the National Bank of America, and move the court to enter an order withholding the mandate in this case because it is the bona fide intention of the appellants to make proper application to the Supreme Court of the United States for a writ of certiorari in this case within 90 days from the date when the decision of this court was rendered herein and in support hereof appellants attach the professional statement of their counsel, Willis C. McMahan of Gary, Indiana.

I hereby certify that it is the bona fide intention of the appellants National Bank of America and David H. Jennings, as Receiver of the National Bank of America, to remove this case to the Supreme Court of the United States by appeal or to make application to said court for a writ of certiorari or do both, as he may be advised, within 90 days from the date when the decision of this court was rendered herein and I further certify and state that I believe there is merit in their case and that the judgment of the United States Circuit Court of Appeals in this case ought to be reversed by the Supreme Court of the United States.

WILLIS C. MCMAHAN,
Counsel for Petitioners.

OSCAR C. STROM,
GEORGE W. HULBERT,
Of Counsel.

Endorsed: Filed June 19, 1934, Frederick G. Campbell, Clerk.

And on the same day, to-wit: On the nineteenth day of June, 1934, the following further proceedings were had and entered of record, to-wit:

Tuesday, June 19, 1934.

Court met pursuant to adjournment and was opened by proclamation.

Before:

Hon. William M. Sparks, Circuit Judge.

National Bank of America, *et al.*, vs. United States Fidelity and Guaranty Company.	Appeal from the District Court of the United States for the Northern District of Indiana, Hammond Division.
5124	

On application of the National Bank of America and David H. Jennings, as Receiver of the National Bank of America, appellants in the above entitled cause by Willis C. McMahan, their counsel, for a stay of execution of the decree of this Court and of the United States District Court for the Northern District of Indiana, Hammond Division, to enable the said National Bank of America and David H. Jennings, as Receiver of the National Bank of America, to apply for and obtain a writ of certiorari from the Supreme Court of the United States, and good cause therefor being shown, It is ordered that the execution and enforcement of said decree be, and it hereby is stayed pending appellants' petition in the Supreme Court of the United States for a writ of certiorari to this court, provided said petition for certiorari is presented with reasonable promptness in said Supreme Court.

UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

I, Frederick G. Campbell, Clerk of the United States Circuit Court of Appeals for the Seventh Circuit, do hereby certify that the foregoing printed pages, numbered from 43 to 60, inclusive, contain a true copy of the proceedings had and papers filed, excepting briefs of counsel, in the case of

National Bank of America and David H. Jennings, as Receiver,

Appellants,

vs.

United States Fidelity & Guaranty Company,

Appellee,

No. 5124, October Term, 1933, as the same remains upon the files and records of the United States Circuit Court of Appeals for the Seventh Circuit.

In Testimony Whereof I hereunto subscribe my name and affix the seal of said United States Circuit Court of Appeals for the Seventh Circuit, at the City of Chicago, this 22nd day of June, A. D. 1934.

FREDERICK G. CAMPBELL,
Clerk of the United States Circuit Court of Appeals for the Seventh Circuit.

(Seal)

[fol. 62] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed October 8, 1934

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Seventh Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

(5659-C)

FILE COPY

AUG 31 1
CHARLES ELMORE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. 338

DAVID H. JENNINGS, Receiver of the National Bank of America, and NATIONAL BANK OF AMERICA, Petitioners,

vs.

UNITED STATES FIDELITY AND GUARANTY COMPANY, Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit and Brief in Support Thereof.

WILLIS C. McMAHAN,
OSCAR C. STROM,
GEORGE W. HULBERT,
JOHN F. ANDERSON,
Attorneys for Petitioners.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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Supreme Court of the United States

OCTOBER TERM, 1934.

No. ——

DAVID H. JENNINGS, Receiver of the National Bank of America, and NATIONAL BANK OF AMERICA, Petitioners,

vs.

UNITED STATES FIDELITY AND GUARANTY COMPANY, Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

To the Honorable Charles Evans Hughes, Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States.

Your petitioners respectfully show:

I.

SUMMARY OF MATTERS INVOLVED.

Nature of Action.

This is a suit in equity brought by the United States Fidelity and Guaranty Company, respondent, in the Circuit

Court of Lake County, Indiana, against the National Bank of America of Gary, Indiana, and David H. Jennings, Receiver of the National Bank of America, to recover $2,196.89 and to have the same declared a preferential claim, that being the amount of a check which had been mailed to and collected by the National Bank of America through the Gary Clearing House before the National Bank of America closed. On petition of Mr. Jennings, as Receiver, the cause was removed to the District Court of the United States for the Northern District of Indiana, Hammond Division (Rec. 5 to 10).

The Facts.

The respondent on the 30th day of December, 1931, received from the Commercial Trust Company of Gary, Indiana, a check payable to its order for $2,196.89 drawn by said Trust Company on The Gary State Bank of Gary, Indiana. On December 30th, 1931, it deposited said check with the Security Trust Company of Indianapolis, Indiana, for collection. The Security Trust Company on the same day deposited said check with the Fletcher American National Bank of Indianapolis for collection, and the last named bank on the same day forwarded said check to the National Bank of America for collection and remittance. The National Bank of America received said check on the morning of December 31st, 1931, and in the forenoon of that day presented it to the drawee bank through the clearing house for collection. There was at that time an organization in Gary known as the Clearing House Association, the sole and only members of said Association at that time being the National Bank of America, The First National Bank, and The Gary State Bank (Rec. 21, 22). It was the custom for the representatives of said banks to meet at ten A. M. on each day and exchange checks received by the member banks before nine thirty A. M. When the clearings were against any bank, it was the custom for such bank to pay such difference to the clearing house by drafts drawn upon its cor-

respondent bank. Prior to nine thirty A. M. of December 31st, 1931, the National Bank of America received from the Fletcher Bank for collection checks drawn on other banks in Gary aggregating $3,661.33, including said check for $2,196.89, and all of said checks were on said day presented by said National Bank of America through the clearing house for exchange and clearance.

When the representatives of the several banks met at the clearing house to exchange checks, the National Bank of America had and presented checks, drawn on The Gary State Bank aggregating $8,095.56, including the said check for $2,196.89. It also had and presented checks drawn on the First National Bank in the sum of $2,329.89, while the other banks held checks drawn on the National Bank of America in the sum of $11,470.19. As a result of the clearings and the exchange of checks on said day, the National Bank of America was indebted to and owed the other banks $1,044.75 for which it drew its draft on the Continental Illinois Bank and Trust Company of Chicago, Illinois, payable to the order of the clearing house (Rec. 22, 23).

After having thus made the collection, the National Bank of America drew and mailed to the Fletcher American Bank its draft on the Continental Illinois Bank and Trust Company for $3,660.83, that being the amount of the proceeds of the checks that day received from the Fletcher American National Bank and so collected through the clearing house. When said last named draft was drawn, the National Bank of America had on deposit with the Continental Illinois Bank and Trust Company an amount in excess of the amount named in said draft (Rec. 24). This draft failed to clear before the National Bank of America failed and for that reason was not paid. At the time the National Bank of America failed, it had on deposit with the Fletcher American National Bank the sum of $3,994.75. On January 5th, 1932, the Fletcher American National Bank charged the account of the National Bank of America with the amount of said draft and later paid the balance of

$333.91 to said receiver and thereafter on demand of the said receiver, it paid him the sum of $3,660.83 and charged the account of the Security Trust Company with the sum of $2,196.89 and the Security Trust Company in turn charged the account of the United States Fidelity and Guaranty Company with the same amount (Rec. 23, 24, 25).

On December 31st, 1931, and for more than two years prior thereto, there was in force in the State of Indiana a statute known as the Uniform Bank Collection Code (Indiana Acts 1929, page 514), the material parts of which statute are set out in the Appendix to the petitioners' brief in support of this petition.

The facts in this cause were stipulated and were adopted by the District Court as its special findings of facts, upon which the court concluded as a matter of law that the cash items of the National Bank of America became impressed with a trust in the sum of $2,196.89 at the time said check was collected; that the petitioner David H. Jennings, as receiver, took said sum impressed with the trust; that respondent was entitled to recover said sum of $2,196.89 with interest thereon in preference to the general creditors of the National Bank of America and judgment was entered in accordance with the conclusions of law. (Rec. 30, 31.)

The receiver of the suspended bank and the bank appealed to the Circuit Court of Appeals, where the judgment of the District Court was reversed as to the item of interest (R. p. 54) and in all other respects affirmed (R. p. 9), and the petitioners seek a review of the decree of the Circuit Court of Appeals holding respondent was entitled to have its claim allowed as preferred.

II.

REASONS RELIED ON FOR ALLOWANCE OF THE WRIT.

The facts having been stipulated, the petitioners complain of the decree, based upon the conclusions of law, wherein it was held:

(1) That there was an augmentation of the funds and assets of the collecting bank when the clearings of the day were against the collecting bank and when the collection item was used for the purpose of paying and taking up checks drawn on the collecting bank.

(2) That when a national bank doing business in Indiana collects, through a clearing house, a check drawn on another bank, when the only thing the collecting bank receives through such collection are checks drawn on itself, there is augmentation of the funds of the collecting bank, and tracing of the proceeds of such collection into the possession of such receiver though the difference in the clearings is against the collecting bank.

(3) That under the Indiana Bank Collection Code, when a collection is made by a national bank in that state through a clearing house, the difference in the clearings being against the bank and when the collection item is used to take up and pay checks drawn on the collecting bank, the funds and assets of the collecting bank are augmented.

Petitioners believe that the writ of certiorari should be granted because:

(a) The decision and decree of the Circuit Court of Appeals involves a federal question relating to the rights of creditors against insolvent national banks under the National Banking Laws and the decision of the Circuit Court of Appeals appears to be in conflict with the principles of law established in analogous cases by this Honorable Court in:

Pottorff v. Texas & Pacific Railroad, 291 U. S. 245, 261 (note 19).
Blakey v. Brinson, 286 U. S. 254, 262.
Schuyler v. Littlefield, 232 U. S. 707, 710, 713.
Cunningham, Trustee, vs. Brown, 265 U. S. 1, 11.
St. Louis & San Francisco R. R. v. Spiller, 274 U. S. 304, 310.
Davis v. Elmira Sav. Bank, 161 U. S. 275.

(b) The decision of the Circuit Court of Appeals is in conflict with the principles of law established by the decisions of the Circuit Courts of Appeal in analogous cases in other circuits, namely:

Second Circuit:
American Can Co. v. Williams, 178 F. 420.

Fourth Circuit:
Ellerbe v. Studebaker Corp., 21 F. (2) 993, 995.

Sixth Circuit:
Brennan v. Tillinghast, 201 F. 609, 612, 613.

Eighth Circuit:
Larabee Flour Mills v. First National Bank, 13 F. (2) 330, 331, cert. den. 273 U. S. 727.
Beard v. Independent District of Pella City, 88 F. 375, 382, 383.
Empire State Surety Co. v. Carroll County, 194 F. 593, 604, 605, 606.
Hirning v. Federal Reserve Bank, 52 F. (2) 382.
Farmers National Bank v. Pribble, 15 F. (2) 175, 176.
Cuttell v. Fluent, 51 F. (2) 974, 976.
Dickson v. First National Bank, 26 F. (2) 411, 412.
Roebeck v. Benedict Flour & Feed Co., 26 F. (2) 440, 441.

Ninth Circuit:
Titlow v. McCormick, 236 F. 209, 211, 212.
Schilling v. Rowe, 64 F. (2) 188, 190.

Tenth Circuit:
Blumenfield v. Union National Bank, 38 F. (2) 455, 457.
Spokane County v. First National Bank, 68 F. 979, 982.

The foregoing cases in the various circuits, and the decisions of this Honorable Court, above cited, establish the principles of law that a preferred claim can be allowed against the estate of an insolvent only where (1) the transaction with the preferred claimant resulted in augmenta-

tion or increase of the assets of the insolvent by the property of the claimant or the proceeds thereof in the form of actual cash or other tangible assets (as distinguished from the establishment and appropriation or dissipation of a deposit or book credit) and (2) that such property or assets of the preferred claimant, or other property identified as being in lieu thereof, can be traced into the hands of the receiver or trustee taking over the assets of the insolvent at the time of suspension or bankruptcy, and (3) that the burden of showing the facts of augmentation and tracing is upon the preferred claimant and that the law will not presume augmentation and tracing. Assuming such principles of law to be controlling in the establishment of preferred claims, it would appear that the decision of the Circuit Court of Appeals is clearly contrary to such principles for the reasons that augmentation and tracing did not exist in the instant case, and the court was in error in its construction of the principles of law relating to augmentation and tracing and also in holding, as a matter of law, that a preferred claim existed regardless of augmentation.

The decision of the Circuit Court of Appeals in the instant case appears to be in conflict, in principle, with its two recent decisions in the cases of Allied Mills, Inc. v. Horton, 65 Fed. (2nd) 708 and Connolly v. Lang, 68 Fed. (2nd) 199.

The decision of the Circuit Court of Appeals in the instant case holding that augmentation and tracing appear where the proceeds of an item held in trust are dissipated through use in a clearings transaction on a day when the balance was against the now insolvent National Bank, is in direct conflict with the decision of the United States Circuit Court of Appeals, Eighth Circuit in Farmers National Bank v. Pribble, cited above, and the cases cited therein.

(c) The Circuit Court of Appeals has decided an important question of general law relating to the liquidation of insolvent national banks, in a way probably untenable and in conflict with the weight of authority indicated by the foregoing decisions.

(d) The precise kind of case decided by the Circuit Court of Appeals has not, apparently, heretofore been passed upon by this Court. The decision of the Circuit Court of Appeals in this case is the first case holding that the Uniform Bank Collection Code applies in the liquidation of an insolvent national bank being liquidated by a receiver and holding that under such statutes, collections made by a national bank are impressed with a trust and that the receivers of such banks holds the assets of such banks in trust without proof of actual augmentation and tracing of the funds.

Eighteen states have adopted the Uniform Bank Collection Code and it is quite important in the liquidation of insolvent national banks that the questions involved in this appeal should be decided by this court so as to furnish an authoritative decision as to whether the funds of a bank are augmented when a collection is made through a clearing house in a state which has adopted a Uniform Collection Code, when the items collected are used to pay an obligation to the clearing house.

(e) The decision and holding of the Circuit Court of Appeals as to the augmentation of the assets of a national bank and the tracing of the proceeds of a collection into the possession of the receiver thereafter appointed for the collecting bank, by holding and deciding that when a national bank doing business in Indiana collects, through a clearing house, a check drawn on another bank, when the only thing the collecting bank receives through such collection are checks drawn on itself, there is an augmentation of the funds of the collecting bank, and a tracing of the proceeds of said collection into the possession of said receiver, though the difference in the clearings is against the collecting bank, on the ground and for the reason that the collecting bank is instantly relieved from the obligation on the checks drawn on itself which it receives in exchange for the checks held for collection and is the equivalent of the substitution

of cash and cash items held by the bank to the extent of the item or check collected, is a decision of a federal question in a way probably in conflict with the decisions of this Honorable Court, and the question of law involved is of great importance to the business world and the legal profession and calls for an authoritative and elucidating decision of this court as to the effect of collections made by a national bank through a clearing house in a state which has adopted the Uniform Bank Collection Code.

WHEREFORE your petitioners pray that a writ of certiorari be issued under the seal of this court directed to the Circuit Court of Appeals for the Seventh Circuit commanding said court to certify and send to this court a full and complete transcript of the record and of the proceedings of said Circuit Court of Appeals, had in the case numbered and titled on the docket as No. 5124, National Bank of America, Appellants v. United States Fidelity and Guaranty Company, Appellee, to the end that this cause may be reviewed and determined by this court and that the decree herein of said Circuit Court of Appeals be reversed by this court and for such further relief as to this court may seem proper.

WILLIS C. McMAHAN,
OSCAR C. STROM,
GEORGE W. HULBERT,
JOHN F. ANDERSON,
Attorneys for Petitioners.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934.

No. ——

DAVID H. JENNINGS, Receiver of the National Bank of America, and NATIONAL BANK OF AMERICA, Petitioners

vs.

UNITED STATES FIDELITY AND GUARANTY COMPANY, Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

OPINION OF COURTS BELOW.

The opinion of the District Court is set out in the Record at pp. 27 to 30 and is reported in 4 Federal Supp. 569. The opinion of the Circuit Court of Appeals for the Seventh Circuit, not yet reported, is found in the record at pp. 46 to 54.

II.

JURISDICTION.

The decree of the Circuit Court of Appeals sought to be reviewed was entered June 4, 1934 (R. 55). Jurisdiction is conferred upon this court to review this cause by writ of certiorari under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925. (U. S. C. Title 28, Section 347.)

This action was commenced by the United States Fidelity and Guaranty Company against the appellants, David H. Jennings, Receiver of the National Bank of America, and the National Bank of America, a banking corporation, organized under the provisions of the National Bank Act and which on January 2nd, 1932, and for many years prior thereto, was engaged in the banking business in the city of Gary, Lake county, Indiana. It is a suit in equity and relates to the winding up of the affairs of an insolvent national bank commenced and brought against an officer, and agent of the United States, namely: David H. Jennings, Receiver of the National Bank of America, and is an action arising under the laws of the United States of America.

III.

STATEMENT OF THE CASE.

A statement of the case is set out in the foregoing petition under the caption, "Summary of Matters Involved," to which reference is here made. Such elaboration of the facts as appears to be pertinent and necessary to the discussion will be indicated where appropriate.

IV.

SPECIFICATION OF ERRORS.

1. The Circuit Court of Appeals erred in holding and deciding that under and by virtue of the act of the General

Assembly of the State of Indiana entitled "An Act to expedite and simplify the collection and payment by banks of checks and other instruments for the payment of money," Approved March 13, 1929, David H. Jennings, as Receiver of the National Bank of America, holds the proceeds of the collection of the check for $2,196.89 in trust and that the same should be paid by him to the United States Fidelity and Guaranty Company in preference to the creditors of said insolvent bank.

2. The court erred in holding and deciding that when a national bank doing business in Indiana receives a check from another bank for collection and remittance, and makes the collection through a clearing house at a time when the difference in the clearings is against the collecting bank, the cash and cash items of the collecting bank are thereby augmented although the check is used in paying the obligation of the collecting bank to the clearing house.

3. The court erred in holding and deciding that when the National Bank of America "exchanged appellee's (United States Fidelity and Guaranty Company's) check on The Gary State Bank for checks which the latter held against the former at the clearing house transaction, appellee's check by virtue of Section 9 of the Indiana Act, was not used to pay the appellant's debt to the clearing house, but was a collection of the check in a manner authorized by the Act; hence that which it received is to be considered as proceeds of the check" and "that the legal effect of the transaction was a substitution of cash and cash items held by appellant bank to the extent of $2,196.89 for the checks upon itself which it received as agent in payment of appellee's check", and by virtue of such transaction "there was augmentation of the cash and cash items to the extent of the proceeds of appellee's check, toward which appellant bank remained a fiduciary." (R. 51, 52.)

4. The Circuit Court of Appeals erred in holding and deciding that "as between the clearing house and appellant

bank, the latter's checks as a matter of commercial convenience were considered rightfully paid under the Indiana law, but as between the bank and appellee, they were not paid by the bank unless it be considered that a corresponding amount of cash was substituted for the unpaid checks."

5. The Circuit Court of Appeals erred in not reversing the trial court's issuance of an injunction restraining the Receiver from using so much of the cash and cash items in his possession as needed to satisfy the judgment and decree appealed from. (R. 31 and 34.)

V.

SUMMARY OF ARGUMENT.

Point 1.

In the liquidation of an insolvent national bank by a receiver appointed by the Comptroller of the Currency the provisions of the *National Bank Act, Section 5236,* U. S. R. S. (12 U. S. C. Ch. 2 Sec. 194) and the decisions of the Federal Courts control and require a pro rata distribution of the assets among all creditors. National banks are instruments designed to be used to aid the government. They are a part of the government's financial system, and their operation and liquidation cannot be controlled by state legislation. The affairs of insolvent national banks in Indiana, as well as elsewhere, are wound up under the National Bank Act as in a code by itself, and the provisions of the Bank Collection Code of Indiana, providing for preferential claims, have no application to insolvent national banks which are being liquidated through a receiver.

Point 2.

A claimant who seeks a preference must establish the fact that the fund from which he seeks payment is his property or the proceeds of his property, or that his property went into it and remains in a mass from which it cannot be

distinguished. Equity will pursue a fund and impose upon it the character of a trust only upon the theory that the money is still the property of the claimant.

Point 3.

It is indispensable to the maintenance of a claim to preferential payment of a receiver of a national bank, that the proof clearly shows that the property which the claimant seeks to recover was impressed with a trust, and that it or its proceeds went into a specific fund or into a specific identified piece of property that came into the hands of the receiver, and also that the value of the general assets of the insolvent bank which came into the possession of the receiver were increased thereby. When a check is collected and paid through a clearing house, the balance of the clearings being against the collecting bank, and the check is used in paying a balance due the clearing house from the collecting bank, the funds in the hands of a receiver of the collecting bank have not been augmented and a claim for preference must fail.

Point 4.

Section 13, subsection 3 of the Indiana Bank Collection Code in so far as it relates to failed or closed national banks, by providing that when such a bank has made a collection and has failed or been closed, the assets of such collecting bank shall be impressed with a trust and that the owner of the item collected shall be entitled to a preferred claim irrespective of whether the funds, representing the item collected can be traced and identified as a part of the assets of the insolvent bank, is an attempt to control and regulate the liquidation of an insolvent national bank in a way which conflicts with the provisions of the *National Bank Act, Section 5236 U. S. R. S.* (12 U. S. C. Ch. 2, Sec. 194) and to that extent is void.

Point 5.

The jurisdiction of the courts is limited to the determination of the validity of a claim of the character here asserted with a direction to the Receiver to certify the claim to the Comptroller of the Currency for payment in due course of administration under the following authorities:

Eastern Township Bank v. Vermont Nat. Bank (C. C.), 22 Fed. 186, 189;
Hallett v. Fish (C. C.), 123 Fed. 201, 203;
Merrill v. First National Bank (C. C. A. 5), 75 Fed. 148, 153;
Richardson v. Louisville Banking Co. (C. C. A. 5), 94 Fed. 442, 449.

The statute (Sec. 194, Title 12, U. S. C. A.) permits claims against insolvent national banks to be proved to the satisfaction of the Comptroller of the Currency or to be adjudicated by a court of competent jurisdiction. Only where a claim, found valid by a court of competent jurisdiction, is certified to the Comptroller of the Currency for payment in due course of administration is there an assurance that the rights of all others similarly situated, who may have proved their claims to the satisfaction of the Comptroller, or in another court, will be protected in the event it is necessary to prorate a given fund between a number of preferred claimants. It was error for the trial court to enjoin the bank Receiver from disposing of the cash that passed into his hands in the manner provided in the National Bank Act (Sec. 192, Title 12, U. S. C. A.) and to direct the Receiver to pay a certain sum forthwith, and this error, properly presented to the Appellate Court, should have been noted and the trial court reversed as was done incident to the erroneous allowance of interest subsequent to suspension. (R. 54.)

ARGUMENT.

Proposition 1.

The National Bank Act and the decisions of the federal courts control in the distribution of the assets of an insolvent national bank. The general rule is that distribution of the assets of a national bank must be made in accordance with *Section 5236 U. S. R. S.* (12 U. S. C. Ch. 2, Sec. 194), which requires a *pro rata* distribution among all creditors.

Of the numerous cases so holding, we cite the following:

Cook County National Bank v. United States, 107 U. S. 445, 448, 27 L. Ed. 537, 538, 539;
Davis v. Elmira Savings Bank, 161 U. S. 275, 284, 286, 40 L. Ed. 700;
Easton v. Iowa, 188 U. S. 220, 229, 47 L. Ed. 452, 456;
First National Bank v. Colby, 88 U. S. 609, 612, 22 L. Ed. 687, 688;
Oates v. National Bank, 100 U. S. 239, 246, 25 L. Ed. 580, 583.

The Controlling Statute.

12 U. S. C. Ch. 2, Sec. 194 is as follows:

> "From time to time, after full provision has been first made for refunding to the United States any deficiency in redeeming the notes of such association, the comptroller shall make a ratable dividend of the money so paid over to him by such receiver on all such claims as may have been proved to his satisfaction or adjudicated in a court of competent jurisdiction, and, as the proceeds of the assets of such association are paid over to him, shall make further dividends on all claims previously proved or adjudicated."

In *Cook County National Bank v. United States*, 107 U. S. 445, 448, 27 L. Ed. 537, 538, the court speaking of the National Bank Act, said:

> "We consider that Act as constituting by itself a complete system for the establishment and government

> of national banks, prescribing the manner in which they may be formed; . . . their liability to be placed in the hands of a receiver, and the manner, in such event, in which their affairs shall be wound up, their circulating notes redeemed and other debts paid or their property applied towards such payment. Everything essential to the formation of the banks, the issue, security and redemption of their notes, the winding up of the institutions and the distribution of their effects, are fully provided for, as in a separate code by itself."

And in the same opinion, the court after quoting the provisions of Section 5236 U. S. R. S. relating to refunding to the United States any deficiency in redeeming the circulating notes of such associations and directing the payment of ratable dividends by the Comptroller on page 450 said:

> "This section provides for the distribution of the entire assets of the bank, giving no preference to any claim except for moneys to reimburse the United States for advance in redeeming the notes."

Davis v. Elmira Savings Bank, 161 U. S. 275, 284, 286, 40 L. Ed. 700, 701, 702; *First National Bank v. Colby*, 88 U. S. 609, 612, 22 L. Ed. 687, 688, are to the same effect.

The issues in the instant case should be determined by resorting to principles of general commercial law, as defined by the federal courts, independent of the state law on the subject.

Easton v. Iowa, 188 U. S. 220, 229, 47 L. Ed. 452, 456;
Farmers & M. National Bank v. Dearing, 91 U. S. 29, 34, 23 L. Ed. 196, 199;
First National Bank v. Selden (C. C. A. 7), 120 F. 212, 215;
Fiman v. State of South Dakota (C. C. A. 8), 29 F. (2) 776;

In *Easton v. Iowa*, 188 U. S. 220, 229, 47 L. Ed. 452, 456, the court, in discussing the nature of national banks and federal legislation creating and regulating them, said:

> "That legislation has in view the erection of a system extending throughout the country and independent so far as powers conferred are concerned, of state legislation which, if permitted to be applicable, might impose limitations and restrictions as various and numerous as the states."

To the same effect see *Farmers & M. National Bank v. Dearing*, 91 U. S. 29, 34, 23 L. Ed. 196, 199.

A state law may be applied to a solvent national bank but not to an insolvent bank in the hands of a Federal receiver. In *First National Bank v. Selden* (C. C. A. 7), 120 F. 212, 215, the court in discussing the application of a state law to an insolvent national bank being liquidated by a receiver, said:

> "Now, while it may be questioned, whether as against the Niles bank, solvent, the Illinois bank might not, as to the payment of check and draft holders, act under the Illinois law as against the law prevailing in federal courts; . . . it is clear that as against the receiver, executing his trust, the federal law alone is applicable. The moment the Niles bank went into the hands of the receiver, the federal law became the law of the distribution of its assets. In no other way could there be unity of administration, and a carrying out of the federal mandate of equality."

To the same effect see *Fiman v. State of South Dakota* (C. C. A. 8), 29 F. (2) 776, 777.

Proposition II.

The adjudicated cases upon the subject of preferred claims have laid down the following prerequisites to the establishment of a preferred claim against an insolvent na-

tional bank: First, the funds claimed must be impressed with a trust. Second, the assets of the bank must have been increased or augmented by the transaction in which the fund was involved. Third, the claimant must be able to trace the fund into the hands of the receiver and there identify same.

American Can Co. v. Williams (C. C. A. 2), 178 Fed. 420-423.
Ellerbe v. Studebaker Corp. (C. C. A. 4), 21 Fed. (2nd) 993-995.
Swan v. Childrens Home Society (C. C. A. 4), 67 Fed. (2nd) 84; Certiorari denied 290 U. S. 704.
City of Miami v. First National Bank (C. C. A. 5), 69 Fed. (2nd) 346.
Keyes v. Pudacah & Illinois Railroad (C. C. A. 6), 61 Fed. (2nd) 611.
Brennan v. Tillinghast (C. C. A. 6), 201 Fed. 609.
Board of Commrs. v. Strawn (C. C. A. 6), 157 Fed. 49-54.
Macy v. Roedenbeck (C. C. A. 8), 227 Fed. 346, 353, 356.
Larabee Flour Mills v. First Nat. Bank (C. C. A. 8), 13 Fed. (2nd) 330-331, Certiorari denied 273 U. S. 727.
Hirning v. Federal Reserve Bank (C. C. A. 8), 52 Fed. (2nd) 382.
Beard v. Independent Dist. (C. C. A. 8), 88 Fed. 375.

Proposition III.

IN RE AUGMENTATION.

In Collections Through Clearing House, There is No Augmentation When the Clearing is Against the Collecting Bank.

Where a collection item is paid through a clearing house, and the balance of the clearings is against the collecting bank, the assets of the bank are not increased for the obvious reason that it receives no actual money on account

of the collection item, but uses the check to pay items in the clearings drawn on it.

The rules relating to augmentation and tracing of the funds of an insolvent national bank are admirably stated in *Empire State Surety Co. v. Carroll County*, 194 F. 593, where the court said:

> "This is a suit in equity against the receiver of a national bank to require him to take from the ratable dividends of other creditors of the bank the requisite amount to pay the county's claim in full. The receiver must make the distribution of the property of this bank in accordance with the provisions of the national banking law. It is the dominant purpose and requirement of that law that, after provision for a redemption of its notes is made, the proceeds of an insolvent national bank shall be equally distributed among its unsecured creditors. So imperative is this provision that it repeals a former act of Congress giving a preference to the United States and annuls a statute of a state giving a preference to deposits of savings bank. *Rev. St. sec. 5236* (U. S. Comp. St. 1901, p. 3508); *Davis v. Elmira Savings Bank*, 161 U. S. 275, 285, 16 Sup. Ct. 502, 40 L. Ed. 700. *National Bank v. Colby*, 21 Wall. 609, 613, 614, 22 L. Ed. 687. The burden, therefore, is on the sureties to prove clearly that they are entitled on equitable principles to the preference they seek. They proved that the bank took the deposits of the county and of its other depositors in trust for them respectively. But this was not enough. They were also required to prove that these deposits or their proceeds, or a certain part of them, came to the hands of the receiver, for he is liable to *cestuis que trustent* to pay trust funds in full only to the extent that he receives them.
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> * * * * * * * * *
>
> "It is indispensable to the maintenance by a *cestui que trust* of a claim to preferential payment by a receiver out of the proceeds of the estate of an insolvent that clear proof be made that the trust property or its

proceeds went into a specific fund or into a specific identified piece of property which came to the hands of the receiver, and then the claim can be sustained to that fund or property only and only to the extent that the trust property or its proceeds went into it. *It is not sufficient to prove that the trust property or its proceeds went into the general assets of the insolvent estate and increased the amount and the value thereof which came to the hands of the receiver.* (Our italics.)

* * * * * * * * *

"In this state of the proof the fact is established, and its existence is not contradicted by any evidence, that the Farmers Bank never obtained or received any of the cash in this $6,368.66 from or on account of the plaintiff's draft for $1,046.89. On the other hand, it expended $115.13 to make the clearance by means of which it used this draft to pay some of the checks and drafts which the People's Bank had against it. . . . The result is that the only effect of the use of the draft of $1,046.89 in the clearance and transaction of May 10, 1924, was not in any way to increase the assets of the Farmers Bank, but possibly, perhaps probably, to diminish its indebtedness or liability by the amount of the draft, and such a reduction of its indebtedness creates no preferential trust in or lien on the assets of the insolvent over the claims of its general creditors.

"But checks of third persons on the bank with which they are deposited which are paid by crediting the bank and charging the drawers on its books fail to increase the cash in its possession and form no basis for a preferential payment to the depositor. *Beard v. Independent District of Pella City,* 88 F. 375, 382, 31 C. C. A. 562.

"Moreover, the deposit of checks of third persons which are credited to the depositor and used by the bank to pay its debts bring no money into its fund of cash and form no foundation for preferential payment to the depositor. *City Bank v. Blackmore,* 75 F. 771, 773, 21 C. C. A. 514.

"Again, checks of third parties deposited with a bank credited to the depositor and collected through a clearing house lay no foundation for a preferential

> payment, in the absence of proof of the actual balance of cash the bank received on account of them, for they may have been and usually are used in whole or in part to discharge the debts of the bank."

To the same effect see, *Cuttell v. Fluent*, 51 F. (2) 975, 976; *Lowell v. Brown*, 284 F. 936, 941; *Blumenfield v. Union National Bank*, 38 F. (2) 455, 457.

The doctrine that a claimed sum may be recovered as a trust fund if it can be traced into the general balance of the assets over liabilities of an insolvent estate has been pronounced an "exploded notion."

> *State Bank of Winfield v. Alva Security Bank*, 232 F. 947;
> *Dudley v. Richards*, 18 F. (2) 876, 878.

Proposition IV.

Section 13, Subsection 3 of the Indiana Bank Collection Code in so far as the same undertakes to provide that the assets of the agent collecting National Bank which has failed shall be impressed with a trust in favor of the owner of the item collected irrespective of whether the funds representing the item collected can be traced and identified as a part of the assets of such failed bank, is in conflict with *Section 5236 U. S. R. S.* (12 U. S. C. Ch. 2, Section 194) and the Indiana Statutes is to that extent void.

To quote from the court's opinion in the leading case on the subject, that of *Davis v. Elmira Savings Bank*, 161 U. S. 275-284:

> "We have, therefore, on the one hand, the statute of the United States, directing that the assets of an insolvent national bank shall be distributed by the Comptroller of the Currency in the manner therein pointed out, that is, ratably among the creditors. We have on the other hand, the statute of the State of New York giving a contrary command. To hold that the state statute is operative is to decide that it overrides the

plain text of the act of Congress. This results, not only from the fact that the two statutes, as we have said, cover the same subject-matter, and relate to the same duty, but also because there is an absolute repugnancy between their provisions, that is between the ratable distribution, commanded by Congress, and the preferential distribution directed by the law of the State of New York.

"The conflict between the spirit and purpose of the two statutes is as pronounced as that which exists between their unambiguous letter. It cannot be doubted that one of the objects of the national bank system was to secure, in the event of insolvency, a just and equal distribution of the assets of national banks among all unsecured creditors, and to prevent such banks from creating preferences in contemplation of insolvency. This public aim in favor of all the citizens of every State of the Union is manifested by the entire context of the national bank act."

One of the most elucidating decisions upon this question is *Prigg vs. Pennsylvania*, 16 Pet. 539, 618 from which we quote: "For if Congress have a constitutional power to regulate a particular subject, and they do actually regulate it in a given manner, and in a certain form, it cannot be that the state legislatures have a right to interfere, and, as it were, by way of complement to the legislation of Congress, to prescribe additional regulations, and what they may deem auxiliary provisions for the same purpose. In such a case, the legislation of Congress in what it does prescribe, manifestly indicated, that it does not intend that there shall be any further legislation to act upon the subject matter. Its silence as to what it does not do is as expressive of what its intention is as the direct provisions made by it."

Proposition V.

This proposition is discussed under Point 5, "Summary of Argument," on page 15 of this brief.

CONCLUSION.

The petitioners believe that the decision of the Circuit Court of Appeals is contrary to the principles of law established in the Circuits other than the Seventh Circuit and to the principles as established by the decisions of this honorable court. The petitioners in the interest of uniformity in the administration of the liquidation of National Banks throughout all of the Circuits and in the interest of settling conclusively the law upon the issues involved submit that their petition for a writ of certiorari should be granted.

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APPENDIX.

Pertinent Sections of the Indiana Bank Collection Code.

An Act to expedite and simplify the collection and payment by banks of checks and other instruments for the payment of money.

Approved March 13, 1929. Indiana Acts 1929, p. 514.

"Section 1. *Be it enacted by the general assembly of the State of Indiana,* That for the purpose of this code:

(a) The term 'bank' shall include any person, firm or corporation engaged in the business of receiving and paying deposits of money within this state. A branch or office or any such bank shall be deemed a bank for the purpose of this act.

(b) The term 'item' means any check, note or other instrument providing for the payment of money."

"Section 2. Except as otherwise provided by agreement and except as to subsequent holders of negotiable instrument payable to bearer or indorsed specially or in blank, where any item is deposited or received for collection, the bank of deposit shall be agent of the depositor for its collection and each subsequent collecting bank shall be subagent of the depositor but shall be authorized to follow the instructions of its immediate forwarding bank and any credit given by any such agent or subagent bank therefor shall be revocable until such time as the proceeds are received in actual money or an unconditional credit given on the books of another bank, which such agent has requested or accepted. Where any such bank allows any revocable credit for an item to be withdrawn, such agency relation shall nevertheless continue except the bank shall have all the rights of an owner thereof against prior and subsequent parties to the extent of the amount withdrawn."

"Section 9. Where ordinary care is exercised, any agent collecting bank may receive in payment of an item without becoming responsible as debtor therefor, whether presented by mail, through the clearing house or over the counter of the drawee or payor, in lieu of money, either (a) the check or draft of the drawee or payor upon another bank or (b)

the check or draft of any other bank upon any bank other than the drawee or payor of the item or (c) such method of settlement as may be customary in a local clearing house or between clearing banks or otherwise: *Provided,* That whenever such agent collecting bank shall request or accept in payment an unconditional credit which has been given to it on the books of the drawee or payor or on the books of any other bank, such agent collecting bank shall become debtor for such item and shall be responsible therefor as if the proceeds were actually received by it in money."

"Section 13. (3) Where an agent collecting bank other than the drawee or payor shall fail or be closed for business as above, after having received in any form the proceeds of an item or items entrusted to it for collection, but without such item or items having been paid or remitted for by it either in money or by an unconditional credit given on its books or on the books of any other bank which has been requested or accepted so as to constitute such failed collecting or other bank debtor therefor, the assets of such agent collecting bank which has failed or been closed for business as above shall be impressed with a trust in favor of the owner or owners of such item or items for the amount of such proceeds and such owner or owners shall be entitled to a preferred claim upon such assets, irrespective of whether the fund representing such item or items can be traced and identified as part of such assets or has been intermingled with or converted into other assets of such failed bank."

"Section 15. In any case not provided for in this act the rules of law and equity, including the law merchant and those rules of law and equity relating to trusts, agency, negotiable instruments and banking, shall continue to apply."

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DEC 10 19

Supreme Court of the United States

OCTOBER TERM, 1934.

No. 338.

DAVID H. JENNINGS, Receiver of the National Bank of America, and National Bank of America, *Petitioners,*

vs.

UNITED STATES FIDELITY AND GUARANTY COMPANY, *Respondent.*

BRIEF OF PETITIONERS.

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(A) Where, as in the instant case, and in the companion cases Nos. 340 and 374, set for argument immediately after this case, a claimant seeks to recover from a Receiver of an insolvent National bank money alleged to have been held by the bank on a trust he must affirmatively establish, under the unmistakable trend and weight of Federal decisions: (1) that his transaction with the bank has resulted in a trust relationship; (2) that the assets of the bank have been augmented or increased by new cash or property accruing from the claimant; (3) that the new property, in its original or changed form, can be traced to the assets taken over by the Receiver at suspension. No augmentation occurs, hence no tracing exists where the transaction results only in a shifting of bookkeeping credits on the books of the now insolvent National bank. No tracing is possible when a check held for collection is used by the collecting bank in payment of its debts.

In the instant case the collection bank never received an identifiable res, an essential to the creation of a trust. Its assets were not augmented because collection was effected through a clearings transaction on a day

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when the balance of clearings was against the collecting bank which debit balance it paid with its Chicago draft and received nothing in the clearings except checks drawn on itself. These checks, when later charged against the drawer's accounts, resulted in mere book-keeping transfers, defeating all possibility of proof of either augmentation or tracing of funds 6

(B) Where, as in the instant case, the record facts establish that neither trust relationship, augmentation, nor tracing appear, the dignity of the claim is in no way increased, nor was it intended to be increased, by the provisions of Sections 1, 2, 9, and 10 of the Indiana Bank Collection Code 15

(C) The jurisdiction of the District Court is limited to the determination of the validity of the trust claim asserted, and to a direction to the Receiver to certify the claim to the Comptroller of the Currency for payment in due course of administration. The court below should have reversed the District Court's order to the Receiver to pay forthwith; should have dissolved the permanent injunction issued by the District Court restraining the Receiver from disposing of the bank's assets as required by the National Bank Act, and should have allowed a general claim.... 32

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UNITED STATES FIDELITY AND GUARANTY COMPANY, *Respondent.*

BRIEF OF PETITIONERS.

I.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals for the Seventh Circuit (Sparks, Circuit Judge) is reported in 71 Fed. (2) 618 and appears in the record at pages 46 to 54. The opinion of the United States District Court, Northern District of Indiana (Slick, D. J.) is reported in 4 Fed. Supp. 569 and appears in the record at pages 27 to 30.

II.

JURISDICTION.

Writ of certiorari was granted on October 8, 1934 (R. 62) under Section 240 (a) of the Judicial Code as amended by the act of February 13, 1925 (U. S. C. Title 28, Section 347)

III.

STATEMENT OF THE CASE.

This is an action, removed from the Lake County Circuit Court of the State of Indiana to the United States District Court for the Northern District of Indiana, (R. 1) wherein the plaintiff, the United States Fidelity & Guaranty Company (respondent here) sued the Receiver of the National Bank of America, Gary, Indiana (petitioner here) to impress a trust upon the assets of the bank that passed to the Receiver. The case was heard upon complaint (R. 2), answer (R. 11), and stipulation of facts (R. 16) resulting in a decree for the plaintiff (R. 30), which was affirmed by the Circuit Court of Appeals for the Seventh Circuit (R. 46 to 54), except that the trial court's allowance of interest, after the bank's suspension, was reversed (R. 54). Petition for writ of certiorari, filed by the bank Receiver was granted October 8, 1934.

The National Bank of America was placed in the hands of an agent of the Comptroller of the Currency for liquidation as an insolvent National bank, prior to the commencement of business, on January 4, 1932. On December 31, 1931, prior to its suspension, this National bank received, through the usual correspondent bank channels, as agent to collect and remit, a check in the amount of $2,196.89, owned by the respondent and drawn on the Gary State Bank of Gary, Indiana (R. 21). On this date the Gary Clearing House Association operated in Gary, the National Bank of America, the First National Bank of Gary (R. 22) and the Gary State Bank being the only members thereof (R. 22). On December 31, 1931, the National Bank of America delivered to the Clearing House checks totaling $10,425.45, including the item of $2,196.89 involved in this action, drawn on other banks, and *received in return checks drawn on the National Bank of America,* totaling $11,470.19 (R. 22, 23). Thereupon the National Bank of America paid its debit clearings balance in the amount of $1,044.75 with

a Chicago draft in accordance with the practice (R. 23). This draft was paid and is not involved in the present suit. In attempted remittance for the respondent's item of $2,196.89, plus other items received from the same correspondent bank, and in accordance with the usual practice, the National Bank of America sent the correspondent bank, located in Indianapolis, its Chicago draft in the amount of $3,660.83, drawn against a sufficient balance, which draft failed of payment because the Chicago bank received notice of the drawer bank's suspension before presentation (R. 24, 25).

In answering the action of the United States Fidelity & Guaranty Company to establish a trust against the bank's assets the bank Receiver admitted that the National bank was agent to collect and remit and that the sum of $2,196.89 was due the plaintiff as a general claim only but denied the trust fund contention on the ground that the assets and funds of the National bank were not augmented or increased by the aforesaid collection through the Clearing House in view of the fact that the clearings resulted in the debit balance against the National bank (R. 22, 23). The District Court held that the cash items of the National bank became impressed with a trust in the plaintiff's favor in the sum of $2,196.89 as a result of the collection of the item in the manner stated and that the Receiver took over this sum of money, subject to the trust (R. 26). The District Court directed the bank Receiver to pay the plaintiff the sum of $2,429.32 (which included interest) forthwith and permanently enjoined him from using so much of the bank's cash and cash items in his hands as might be necessary to satisfy the decree. The Circuit Court of Appeals held that as a result of the collection through the clearing house in the manner stated, a trust in the plaintiff's favor, in the sum of $2,196.89 attached to the cash and cash items of the collecting National bank (R. 51, 52); that the assets of the collecting bank were augmented; that the proceeds are traceable into the hands of the Receiver (R. 54) and

that the dignity of the plaintiff's claim against the National bank was increased by certain provisions of the Indiana Bank Collection Code, particularly Section 9 thereof. The Circuit Court of Appeals reversed the District Court's allowance of interest.

IV.

SPECIFICATION OF ERRORS.

(a) The Circuit Court of Appeals erred in holding that the relationship of principal and agent, admittedly existing between the respondent and the collecting National bank, ever became that of trustee and cestui que trust.

(b) The Circuit Court of Appeals erred in holding that the collection transaction augmented the assets of the collecting National bank.

(c) The Circuit Court of Appeals erred in holding that the proceeds of the collection transaction are traceable into the hands of the bank Receiver.

(d) The Circuit Court of Appeals erred in not holding that the respondent's claim against the bank Receiver is a general claim only.

(e) The Circuit Court of Appeals erred in holding that the dignity of the respondent's claim against the bank Receiver was increased in any manner by the provisions of Sections 1, 2, 9, and 10 of the Indiana Bank Collection Code.

(f) The Circuit Court of Appeals erred in not reversing the District Court's direction to the bank Receiver to pay the plaintiff forthwith the sum of $2,429.32 or any other sum except on the basis of allowance of a general claim and payment of pro rata dividends thereon.

(g) The Circuit Court of Appeals erred in not dissolving the permanent injunction issued by the District Court restraining the bank Receiver from using so much of the bank's cash and cash items in his possession as is needed to satisfy the decree.

V.

SUMMARY OF ARGUMENT.

(A) Where, as in the instant case, a claimant seeks to recover from a Receiver of an insolvent National bank money alleged to have been held by the bank on a trust he must affirmatively establish, under the unmistakable trend and weight of Federal decisions: (1) that his transaction with the bank has resulted in a trust relationship; (2) that the assets of the bank have been augmented or increased by new cash or property accruing from the claimant; (3) that the new property, in its original or changed form, can be traced to the assets taken over by the Receiver at suspension. No augmentation occurs, hence no tracing exists where the transaction results only in a shifting of bookkeeping credits on the books of the now insolvent National bank. No tracing is possible when a check held for collection is used by the collecting bank in payment of its debts.

In the instant case the collecting bank never received an identifiable res, an essential to the creation of a trust. Its assets were not augmented because collection was effected through a clearings transaction on a day when the balance of clearings was against the collecting bank which debit balance it paid with its Chicago draft and received nothing in the clearings except checks drawn on itself. These checks, when later charged against the drawer's accounts, resulted in mere bookkeeping transfers, defeating all possibility of proof of either augmentation or tracing of funds.

(B) Where, as in the instant case, the record facts establish that neither trust relationship, augmentation, nor tracing appear, the dignity of the claim is in no way increased, nor was it intended to be increased, by the provisions of Sections 1, 2, 9, and 10 of the Indiana Bank Collection Code.

(C) The jurisdiction of the District Court is limited to the determination of the validity of the trust claim asserted,

and to a direction to the Receiver to certify the claim to the Comptroller of the Currency for payment in due course of administration. The court below should have reversed the District Court's order to the Receiver to pay forthwith; should have dissolved the permanent injunction issued by the District Court restraining the Receiver from disposing of the bank's assets as required by the National Bank Act and should have allowed a general claim.

VI.

ARGUMENT.

(A) Where, as in the instant case, and in the companion cases Nos. 340 and 374, set for argument immediately after this case, a claimant seeks to recover from a Receiver of an insolvent National bank money alleged to have been held by the bank on a trust, he must affirmatively establish, under the unmistakable trend and weight of Federal decisions: (1) that his transaction with the bank has resulted in a trust relationship; (2) that the assets of the bank have been augmented or increased by new cash or property accruing from the claimant; (3) that the new property, in its original or changed form, can be traced to the assets taken over by the Receiver at suspension. No augmentation occurs, hence no tracing exists where the transaction results only in a shifting of bookkeeping credits on the books of the now insolvent National bank. No tracing is possible when a check held for collection is used by the collecting bank in payment of its debts.

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in mere bookkeeping transfers, defeating all possibility of proof of either augmentation or tracing of funds.

The mandate of the National Bank Act requires a pro rata distribution of the assets of an insolvent National bank among all creditors. This mandate can be avoided by the respondent only upon affirmative proof of trust relationship, augmentation, and tracing of funds to the Receiver.

Section 5236 U. S. R. S. (12 U. S. C. Ch. 2, Sec. 194) (Appendix p. 40) requires a pro rata distribution of an insolvent National bank's assets among all its creditors. In referring to this section this court said in Cook County National Bank v. United States, 107 U. S. 445, 450, that it

> "*provides for the distribution of the entire assets of the bank,* giving no preference to any claim except for moneys to reimburse the United States for advances in redeeming the notes. When this reimbursement is fully provided for, the balance of the assets, as the proceeds are received, is subject to a ratable dividend on all claims proved to the satisfaction of the receiver, or adjudicated by a court of competent jurisdiction."

Even the United States as a sovereign is a general creditor only, unless it has taken the security provided by law, except for advances to redeem the circulating notes and in minor instances involving certified checks given for customs duties and certain taxes. (19 U. S. C. Ch. 3, sec. 198; 26 U. S. C. Ch. 3, sec. 109). The circulating notes are required to be adequately secured at all times and the debtor continues to be primarily liable for the taxes and duties and consequently the exceptions are very rarely applicable.

The respondent can avoid participation in the pro rata distribution provided by the National Bank Act only upon a showing that the assets that passed into the hands of the Receiver for the benefit of all creditors included the identifiable property of the claimant or its proceeds. The re-

spondent must show, *by the burden of proof*, that as a result of its transaction the bank, before suspension, (a) received property of the claimant in trust, (b) that the property so received actually augmented the existing assets of the bank by way of adding thereto cash or other property (as distinguished from the addition of a bookkeeping credit) and (c) that the augmented assets, in their original or changed form passed into the hands of the Receiver.

Unless the record contains affirmative proof by the respondent of trust relationship, augmentation and tracing of funds to the Receiver the trust claim fails because all doubts must be resolved in favor of the bank Receiver who is the trustee for general creditors. As stated by this court in Texas & Pacific Railway v. Pottorff, 291 U. S. 245, 261, Note 19, decided at the last term:

> "The claimant has the burden of identifying the property in its original or altered form. Schuyler v. Littlefield, 232 U. S. 707. It is not enough to show that at the time of receipt the general assets of the insolvent were increased or that debts were discharged. Wuerpel v. Trust Co., 238 Fed. 269, 272-3; Knauth v. Knight, 255 Fed. 677; State Bank of Winfield v. Alva Security Bank, 232 Fed. 847; In re See, 209 Fed. 172; In re Dorr, 196 Fed. 292; City Bank v. Blackmore, 75 Fed. 771; compare Railway v. Spiller, 274 U. S. 304, 311; Cunningham v. Brown, 265 U. S. 1."

In its opinion in Schuyler v. Littlefield, 232 U. S. 707, this court said, at page 713:

> "All these claims were disallowed because of the failure to make the requisite proof. Our investigation of the facts leads us to the same conclusion so far as concerns the appellants' claim. They were practically asserting title to $9600 said to have been traced into stock in the possession of the Trustee. Like all other persons similarly situated, they were under the burden of proving their title. If they were unable to carry the burden of identifying the fund as represent-

ing the proceeds of their Interborough stock their claim must fail. If their evidence left the matter of identification in doubt the doubt must be resolved in favor of the trustee, who represents all of the creditors of Brown & Co., some of whom appear to have suffered in the same way. Like them, the appellants must be remitted to the general fund."

For a summarized statement of the principles of law applicable to these claims in a case wherein the facts are substantially the same as those presented in the instant case, the following excerpt is quoted from the opinion of the Circuit Court of Appeals for the Eighth Circuit in Farmers National Bank v. Pribble, 15 Fed. (2nd) 175-176:

"It is clear that counsel for the plaintiff were familiar with and probably had before them when they drew this complaint the established rule in the federal courts prescribing the facts requisite to establish a cause of action by a *cestui que trust* to recover from the receiver of the property of an insolvent corporation the payment in full of a trust fund in his possession in preference to the payment of anything to its general creditors, for they pleaded and set forth such facts in the complaint as stated a perfect cause of action in accordance with that rule, which is:

" 'It is indispensable to the maintenance by a *cestui que trust* of a claim to preferential payment (by a receiver) out of the proceeds of the estate of an insolvent that clear proof be made that the trust property or its proceeds went into a specific fund or into a specific identified piece of property which came to the hands of the receiver, and then the claim can be sustained to that fund or property only, and only to the extent that the trust property or its proceeds went into it. It is not sufficient to prove that the trust property or its proceeds went into the general assets of the insolvent estate and increased the amount and value thereof which came to the hands of the receiver.' Empire State Surety Co. v. Carroll County, 194 F. 593, 114 C. C. A. 435; and cases there cited; Beard v. Independent School District, 88 F. 375, 31 C. C. A. 562; In re Seven Corners

Bank, 58 Minn. 5, 59 N. W. 633; American Can Co. v. Williams (C. C.), 176 F. 816; Willoughby v. Weinberger, 15 Okl. 226, 79 P. 777; Macy v. Roedenbeck, 227 F. 347, 356; 142 C. C. A. 42, L. R. A. 1916 C, 12; Central Trust Co. v. Chicago, A. & N. Ry. Co. (D. C.), 232 F. 936, 943; State Bank of Winfield v. Alva Security Bank, 232 F. 847, 849, 147 C. C. A. 41; Titlow v. McCormick, 236 F. 209, 149 C. C. A. 399; Zenor v. McFarlin, 238 F. 721, 725, 151 C. C. A. 571; Scullin Steel Co. v. North American Co., 255 F. 945, 947, 167 C. C. A. 237; Mechanics & Metals Nat. Bank v. Buchanan (C. C. A.), 12 F. (2d) 891.

The doctrine that a *cestui que trust,* whose property had helped to swell the general assets of a corporation which was or became insolvent, has a prior right or interest in those general assets, without specific identification and tracing of such claimant's property, was again expressly repudiated by this court in the case last cited. *The fact that the claimant's property paid or reduced the indebtedness or liability of the insolvent corporation, so that it will pay a larger percentage of its debts, justifies no lien on its assets by or preference in payment to the cestui que trust* (1) because such a reduction of indebtedness does not increase the property or the value of the property of the insolvent; and (2) because the property of the claimant so used to pay a part of the insolvent's general indebtedness or liability never goes into, and therefore cannot be traced into, the property or assets of the insolvent which subsequently come into the possession of the receiver. Titlow v. McCormick, 236 F. 209, 149 (C. C. A.) 399; American Can Co. v. Williams (C. C.), 176 F. 816; Lucas County v. Jamison (C. C.), 170 F. 338; Multnomah v. Oregon National Bank (C. C.), 61 F. 912; Beard v. Independent School District, 88 F. 375, 31 C. C. A. 562; Hecker-Jones-Jewell Mill Co. v. Cosmopolitan Trust Co., 242 Mass. 181, 136 N. E. 333, 24 A. L. R. 1148. (Italics inserted)

The case of Schilling v. Rowe (C. C. A. 9), 64 Fed. (2nd) 188, 190, involved facts similar to those presented in the instant case, the collection having been effected through a clearing house transaction on a day when the balance in

the clearings was against the collecting bank. In classifying the claim as general only the court said in its opinion at page 190:

> "*The authorities are uniform* that where checks held by a bank in its trust capacity are used by the bank to pay indebtedness due from it to other banks on account of negotiable paper held by them through the ordinary process of clearings, or otherwise, that there is no augmentation of the assets which come into the hands of the receiver within the rule making the priority of the beneficiary depend upon such augmentation." (Italics inserted)

In Dickson v. First National Bank (C. C. A. 8), 26 Fed. (2nd) 411, two checks were collected through a clearings transaction on a day when the balance was against the collecting bank. In its opinion at page 412 the court said:

> "The ultimate result was that the indebtedness of the defendant bank was decreased to the amount of these two checks. The transaction did not in any sense result in increasing the assets of the bank which were available for distribution to creditors. *To grant plaintiff a preference would not be to authorize him to take from the assets something which rightfully belonged to him by reason of his property being wrongfully added to the assets, but it would permit him to take from the assets funds which belong to other creditors.*" (Italics inserted)

To the same effect under similar factual situations are:

Rorebeck v. Benedict Flour & Feed Co., (C. C. A.) 26 Fed. (2) 440, 441.
City Bank v. Blackmore, ~~76~~ 75 Fed. 771, 773.
Empire State Surety Co. v. Carroll County (C. C. A. 8), 194 Fed. 593, 603, 604, 606.
Spokane Co. v. First National Bank (C. C. A. 9), 68 Fed. 979, 982.
Nyssa-Arcadia Drainage Dist. v. First National Bank, 3 Fed. (2nd) 648.
American Can Co. v. Williams (C. C. A. 2), 178 Fed. 420, 422.

First National Bank v. Williams (D. C. N. C.), 15 Fed. (2) 585, 587. (Opinion by Circuit Judge Parker sitting as District Judge.)
Smith Reduction Corp. v. Williams (D. C. N. C.), 15 Fed. (2) 874. (Opinion by Circuit Judge Parker sitting as District Judge.)

In the instant case the respondent can establish a general claim only because the original relationship of principal and agent, admittedly existing between the parties, never became that of trustee and *cestui que trust*. The collecting bank received nothing as a result of the collection of the respondent's item through the Clearing House except checks drawn on itself. These checks, drawn against credit balances then on the books of the collecting National bank, when charged to the depositors' accounts, resulted in mere transfers of bookkeeping credits which did not create a res, an essential to a trust. A trust cannot exist unless there is a res, *i. e.*, property to which the trust pertains. (American Law Institute, Trusts Restatement, Section 70.) A debt owing by the collecting bank to either its depositors or the forwarder of the collection item cannot become a trust res because "An obligor cannot be trustee either of his duties or of the obligee's rights under the obligation." (American Law Institute, Trusts Restatement, Section 75, and comment "a" and illustration thereto.) As stated by this court in Blakey v. Brinson, 286 U. S. 254, 263, in discussing similar transfers of credit:

> "The cancellation of the credit balance by the debit neither suggests any intention to establish a trust nor points to any identifiable thing which could be the subject of it."

In the instant case the respondent's collection item was dissipated through use by the collecting bank in a clearings transaction on a day when it had a debit balance. These facts defeat the trust, augmentation, and tracing of funds contentions but the respondent asserts (respondent's brief

in opposition to petition for certiorari, page 4) that the collecting bank received checks drawn on itself ($11,470.19, R. 23) in payment of the collection item. Even on this theory the collection proceeds consisted of checks drawn on the now insolvent National bank which, as already stated, could not be the subject of a trust. In a recent case in the Circuit Court of Appeals for the Eighth Circuit—Hirning v. Federal Reserve Bank, 52 Fed. (2nd) 382, 386—the Court, in discussing these principles, said:

> "It is contended by the appellee that the checks sent by the Reserve Bank to the Brookings Bank constituted a trust fund, and that this trust fund has been traced into the currency and collection items sent by the Brookings Bank to the Reserve Bank.
>
> "The trial court seems to have adopted this view as one of the grounds of its decision in ordering judgment for defendant.
>
> "We do not agree with this contention. It must be remembered that the checks sent to the Brookings Bank by the Reserve Bank were all of them checks drawn on the Brookings Bank. *When the Brookings Bank accepted the checks, this produced no additional funds in its hands. Its assets were not augmented. No trust fund was created. If there was no trust fund, there could, of course, be no tracing of the trust fund into any assets of the Brookings Bank.* The doctrine that a trust fund is created when checks drawn on bank A by bank B for collection, *i. e.*, for payment, has been disapproved by the decisions in this Circuit, *as has also the doctrine that the forwarding bank or its principal has a general lien on the assets of the drawee bank* for the payment of such checks. Rorebeck v. Benedict, etc. Co., 26 Fed. (2nd) 440; Farmers National Bank v. Pribble, 15 Fed. (2nd) 175; Larabee Flour Mills v. First Nat. Bank, 13 Fed. (2nd) 330; Macy v. Roedenbeck, 227 Fed. 346, 352; Beard v. Independent Dist., 88 Fed. 375." (Italics inserted)

To the same effect are the following excerpts from opinions of the Circuit Courts of Appeal for the Fourth and Fifth Circuits:

Anheuser-Busch Brewing Ass'n v. Clayton, (C. C. A. 5), 56 Fed. 759-60:

"The relation between appellant and the McNab Bank as to the draft on Morris sent by the former to the latter for collection was that of principal and agent; but, in order to enforce a trust in favor of appellant as to any money collected on said draft, it must be specifically traceable into the hands of the receiver. Commercial Nat. Bank v. Armstrong, 39 Fed. Rep. 684; same case in Supreme Court of the United States (Oct. term, 1892; not yet officially reported, 13 Sup. Ct. Rep. 533). *Accepting Morris' check in payment of his debt to appellant, and charging the amount of it on Morris' account by the bank, was but a shifting of its liability, whereby it became appellant's debtor,* and assumed the obligation to pay to it the amount of the check less exchange. There is nothing to indicate that this amount was separated and kept unmingled with the bank's own money; but, on the contrary, it is conceded that it is undistinguishable from the mass of the bank's own money, and cannot be traced to and identified in the hands of the receiver. This being so, appellant has no better equity than the other creditors of the bank, and is entitled to no priority over them. It can only come in as a general creditor, * * *" (Italics inserted)

Ellerbe v. Studebaker Corp. (C. C. A. 4), 21 Fed. (2nd) 993:

"In ordinary cases, of course, the receipt by the collecting bank of a check drawn against the account of one of its depositors does not bring anything into the bank, and cannot be said to augment in any way assets passing into the hands of the Receiver. It is a mere shifting of credits. Larabee Mills v. First Nat. Bank (C. C. A. 8th), 13 Fed. (2nd) 330; American Can Co. v. Williams (C. C. A. 2), 178 Fed. 420; North Carolina Corp. Com. v. Merchants & Farmers Bank, 137 N. C. 697, 50 S. E. 308."

A claim for a trust status against the assets of an insolvent National bank, based upon a transfer of bookkeeping credits was classified as general only by the Circuit

Court of Appeals for the Fifth Circuit in its recent decision in First National Bank of St. Petersburg v. City of Miami, 69 Fed. (2nd) 346, a case that was twice certified to this court and argued on one occasion, the certificates being dismissed on jurisdictional grounds. The court said in its opinion (p. 347):

> "As proven, no sum whatever was collected and held for plaintiff by the St. Petersburg bank to which a trust could attach. In this state of the proof to hold the bank as trustee would be to hold it a trustee not of a thing, but of a claim against itself, a holding on its face so artificial and unreal as to be impossible."

The bank Receiver submits that in this case, as in Blakey v. Brinson, 286 U. S. 254, the claim should be classified as general only because of the failure to establish a relationship of trustee and cestui que trust.

(B) Where, as in the instant case, the record facts establish that neither trust relationship, augmentation, nor tracing appear, the dignity of the claim is in no way increased, nor was it intended to be increased, by the provisions of Sections 1, 2, 9, and 10 of the Indiana Bank Collection Code.

Sections 1, 2, 9 and 10 of the Indiana Bank Collection Code were not intended to and do not alter or modify the Federal rule stated under "A" above.

In its opinion the court below recognizes the Federal rule discussed under "A" above, which classifies the respondent's claim as general only, but undertakes to avoid it in the instant case by a finding (R 48) that:

> "Whether a trust relationship existed between the bank and appellee, by virtue of the circumstances hereinbefore set forth, is to be determined by sections 1, 2, 9, and 10 of the Indiana Uniform Bank Collection Code, ch. 164, Indiana Acts, 1929."

It has always been the position of the Comptroller of the Currency and it is the position of the bank Receiver in this case that all of the provisions of the Bank Collection Code, adopted in 18 States, are applicable to the transactions of National banks doing business in those States, except Section 13 of this Code, and, as more fully hereinafter indicated, it is believed Section 13 is inapplicable to insolvent National banks because it is in conflict with the pro rata distribution mandate of Congress (Sec. 194, Title 12 U. S. C.) (Appendix p. 40) and with the decisions of this court in Davis v. Elmira Savings Bank, 161 U. S. 275, 283, 284, 286; Easton v. Iowa, 188 U. S. 220, 229; and Cook County National Bank v. United States, 107 U. S. 445. "But a National bank is subject to State law unless that law interferes with the purposes of its creation, or destroys its efficiency, or is in conflict with some paramount Federal law." Lewis v. Fidelity Company, 292 U. S. 559, 566. For convenience of reference the complete Bank Collection Code is printed in the appendix (pages 41 to 58), together with a foreword and comment, section by section, by its proponents. A full discussion of this code, section by section, is contained in a series of articles by Wayne L. Townsend, Professor of Law, Western Reserve University, in the Tulane Law Review, Volume VIII, Nos. 1, 2, and 3, Dec. 1933, Feb. 1934, April 1934.

Petitioner contends, however, that nothing contained in Sections 1, 2, 9 and 10 of the Bank Collection Code lends support to the conclusion of the court below that the Legislature intended to impress a trust, in favor of the collection item forwarder, upon the cash and cash items of the collecting bank. The only sections of the Code intended to give the collection item *forwarder* protection against the contingency of insolvency are Sections 11, 12 and 13 and the only section intended to impress a trust upon the assets of the collecting bank in favor of the collection item forwarder is Section 13. Section 13 is designated by its framers (Appendix p. 49) "Insolvency and Preferences."

Subdivision 1 of Section 13 becomes effective "When the drawee or payor or any other agent collecting bank shall fail or be closed for business." Subdivision 2 of Section 13 becomes effective when the "drawee or payor shall fail or close for business as above." Subdivision 3 of Section 13 becomes effective "Where an agent collecting bank other than the drawee or payor shall fail or be closed for business as above."

Under the plain language of the Section the trust provided therein does not come into being except in the event of insolvency. Accordingly the section is void as to National banks under the following excerpt from the opinion of this court in Davis v. Elmira Savings Bank, 161 U. S. 275, 283:

> "It is clear that these two statutes cover exactly the same subject matter. Both relate to insolvent banks; both ordain that the right of preference on the one side and the duty of ratable distribution on the other shall only result from insolvency; both cover the assets of such banks coming, after insolvency, into the hands of the officer or person authorized to administer them. It is equally certain that both statutes relate to the same duty on the part of the officer of the insolvent bank; the one directs the representative to make a ratable distribution; the other requires, if necessary, the application of the entire assets to payment in full, by preference and priority over all others of a particular and selected class of creditors therein named. We have, therefore, on the one hand, the statute of the United States, directing that the assets of an insolvent national bank shall be distributed by the Comptroller of the Currency in the manner therein pointed out, that is, ratably among the creditors. We have on the other hand, the statute of the State of New York giving a contrary command. To hold that the State statute is operative is to decide that it overrides the plain text of the Act of Congress. This results, not only from the fact that the two statutes, as we have said, cover the same subject-matter, and relate to the same duty, but also because there is an absolute repugnancy between

their provisions, that is, between the ratable distribution, commanded by Congress, and the preferential distribution directed by the law of the State of New York.

The Circuit Court of Appeals for the Second Circuit held Section 13 of the Bank Collection Code inapplicable to insolvent National banks, in its recent decision in Old Company's Lehigh, Inc. v. Meeker, Receiver of the First National Bank of Mamaroneck, 71 Fed. (2nd) 280. This case is now pending in this court on the merits (No. 340) and the bank Receiver's brief therein (P. 2.1.) lists additional cases for the proposition that Section 13 of the Code is inapplicable to National banks.

The respondent in the instant case concedes (p. 3, Respondent's brief in opposition to petition for certiorari) that it does not rely on Section 13 of the Code. The court below did not rely on Section 13 to establish a trust. The bank Receiver admits that the relationship of principal and agent between the parties continued at all times until the bank's suspension. Consequently, the principal question before this court is whether or not the dignity of the respondent's claim is increased by Section 9 of the Code, (Sec. 3861.9 Vol. IV Burns' Ann. Ind. Stat., 1929 Supp.) which reads as follows:

> "Where ordinary care is exercised, any agent collecting bank may receive in payment of an item without becoming responsible as debtor therefor, whether presented by mail, through the clearing house or over the counter of the drawee or payor, in lieu of money, either (a) the check or draft of the drawee or payor upon another bank or (b) the check or draft of any other bank upon any bank other than the drawee or payor of the item or (c) such method of settlement as may be customary in a local clearing house or between clearing banks or otherwise; provided that whenever such agent collecting bank shall request or accept in payment an unconditional credit which has been given to it on the books of the drawee or payor or on the books of any other bank, such agent collecting bank

shall become debtor for such item and shall be responsible therefor as if the proceeds were actually received by it in money."

The views of the court below concerning the effect of Section 9 of the Bank Collection Code summarize the issues now before this court, and hence are quoted from its opinion (R. 51, 52):

> "Appellee argues that when appellant bank exchanged appellee's check on the Gary State Bank for checks which the latter held against the former at the clearing house transaction, appellee's check, by virtue of section 9 of the Indiana Act, was not used to pay the appellant's debt to the clearing house, but it was a collection of the check in a manner authorized by the Act; *hence that which it received is to be considered as proceeds of the check*, and since appellant bank did not request or accept an unconditional credit for the item on the books of the Gary State Bank, or of any other bank, as provided under section 9, the bank did not become responsible as debtor for either the check or its proceeds, but it still was liable as agent. *It further contends that the proceeds thus received in payment were the same as cash to appellant bank and were in contemplation of section 9 automatically reflected in the cash and cash items of that bank*, after the clearing house transaction, because the cash and cash items became instantly relieved from the obligations of the checks received in exchange to the extent of appellee's check, and that the legal effect of the transaction was a substitution of cash and cash items held by appellant bank to the extent of $2196.89 for checks upon itself which it received as agent in payment of appellee's check. Hence it says there was augmentation of the cash and cash items to the extent of the proceeds of appellee's check toward which appellant bank remained as fiduciary.
>
> "*We are in accord with appellee's contention in this respect.*" (Italics inserted)

Petitioner contends section 9 has no such purpose or effect. The language of Section 9 is exact and leaves no

room for construction. *Its purpose, in plainly expressed language, is to protect the collecting bank against a liability as debtor where it accepts something other than cash as the collection proceeds. The section protects the collecting bank and not the collection item owner.* The draft of the proponents of this legislation (App. 47) states the purpose of each section. Before Section 9 (App. 47) appears the statement "Medium of Payment". The intent of Section 9 is stated by the framers of the Act in the explanatory note (App. 56) to be:

> "The principle of Section 9 is to authorize the agent collecting bank to receive, instead of money, without being responsible therefor as debtor, the customary method of settlement for an item by draft on another bank or by exchange of items and settlement of balance by money or draft."

The purpose of section 9 is clearly understood when it is read in the light of this court's opinion in Federal Reserve Bank v. Malloy, (1924) 264 U. S. 160, which held that, in the absence of any instruction or permission from the owner of a check, or any custom brought to the notice of such owner, to the contrary, the bank has no authority to accept or receive in payment of a check indorsed to it for collection, anything other than money. This court held (page 167) that Regulation "J" of the Federal Reserve Board, 1920, "does not expressly permit the acceptance of payment other than in money." Thereafter, and in 1924, Regulation "J" of the Federal Reserve Board was amended to avoid the rule of the Malloy case and today, after subsequent amendments, reads in part, as follows:

> "The Federal Reserve Bank may, in its discretion and at its option, either directly or through or from an agent, accept in payment of or in remittance for such checks, cash, bank drafts, transfers of funds or bank credits, or other forms of payment or remittance, acceptable to the collecting Federal Reserve Bank. The Federal Reserve Bank shall not be liable for the fail-

> ure of the drawee bank or any agent to pay or remit for such checks, nor for any loss resulting from the acceptance from the drawee bank or any collecting agent, in lieu of cash, of any other form of payment of remittance authorized herein, nor for the nonpayment of, or failure to realize upon, any bank draft or other medium of payment or remittance which may be accepted from the drawee bank or any collecting agent."

This avoidance of the Malloy rule by the Federal Reserve Banks, the largest check collection agencies in the United States, resulted in a similar avoidance by practically all large banks through contracts with their customers. In this connection the following excerpt is quoted from Section 1451 a, Vol. 2, Paton's Digest (1926), (reference volumes found in most banks), edited and compiled by Thomas B. Paton, Jr., Assistant General Counsel of the American Bankers Association, who assisted in drafting the Uniform Bank Collection Code. (Appendix p. 41)

> "The Malloy decision, 264 U. S. 160, 68 L. ed. 617, 44 Sup. Ct. (1924) 296, 31 A. L. R. 1261 and note, confirms the need for a change in the passbook rules or other collection agreement to express authorization to the bank receiving checks on deposit for collection to accept the drawee's draft as payment in lieu of cash. A standard form of depositor's agreement is printed in 1446, which agreement was drafted to correct the undue burden assumed by a bank accepting collection items for deposit. *It was drafted since and in the light of the Malloy decision, and is recommended to all banks for their use.*" (Italics inserted)

Section 9 of the Bank Collection Code merely reduced to statutory form the protection collecting banks already enjoyed, and now enjoy in non-collection code States through contract, against becoming liable as debtor where something other than money was accepted as the collection proceeds. Nothing contained in the Section, or its history, gives support to the conclusion reached by the court below

that it was intended to attach a trust to the cash or cash items of the collecting bank in favor of the collection item owner. The section contemplates that collection will be effected in the usual course of the banking business and that the collecting bank will remit the proceeds by its credit instrument. The collection transaction involved in the instant case was handled exactly as contemplated by this section and the other sections of the Act. *The collecting National bank had no duty to segregate its assets in trust for the respondent, after collection was effected in the manner made, and it did not segregate assets to be held in trust for the respondent.* The section gives no suggestion that a lien on the collecting bank's assets was intended to result therefrom. As agent to collect, the collecting bank received nothing from the transaction except items drawn on itself. These items represented mere transfers of bookkeeping credits, which could not be the subject of a trust. Consequently a trust relationship never came into existence. As collecting agent the national bank, and now its Receiver, must account for what it received and this the Receiver has always been willing to do by allowing the respondent a general claim.

Even if the State Legislature had, (which we deny) by the use of plain language, affixed a lien to the collecting bank's assets prior to suspension, by the provisions of Sections 9 or 13 of the Bank Collection Code the result would be the same—a general claim only, for the reason that a National bank is without power to give security for a *private* deposit. Texas & Pacific Railroad v. Pottorff, 291 U. S. 245. An attempt to secure a *private* depositor or his assignee by lien or otherwise would be absolutely void. Under the respondent's theory in the instant case the collection proceeds consisted of checks drawn on the now insolvent National bank. When these checks were charged to the depositors' accounts private deposit balances were assigned. Hence *the legal position of the respondent is*

that of assignee of a private deposit balance. The State statute could give no power to a National bank, consequently it would be inapplicable to such a bank. The National Bank Act empowers National banks to give security for public deposits, consequently the respondent receives no assistance from this court's opinion in Lewis v. Fidelity & Deposit Company, 292 U. S. 559.

In Royal Manufacturing Company v. Spradlin, 6 Fed. Sup. 98, the District Court allowed a priority claim against an insolvent National bank on the lien theory, the North Carolina statute involved (Sec. 218(c) (14) N. C. Code 1927) being substantially different and much more favorable to the trust claimant's contentions than any provision of the Bank Collection Code. The proposition stated in this paragraph was there urged in the bank Receiver's brief on appeal. The Circuit Court of Appeals of the Fourth Circuit in reversing the District Court and classifying the claim as general only in its very recent and as yet unreported opinion dated November 19, 1934 (Parker, C. J.) (Appendix pp. 59-61) said:

> "It is clear, we think, that even if this proviso be construed as having relation to solvent banks as distinguished from those in liquidation, it cannot affect national banks. It has been held that these banks have no power to pledge their assets to secure a private deposit (Texas Pac. Ry. v. Pottorff, 291 U. S. 245, 253); and one of the reasons for this holding is that to permit such pledge would be inconsistent with many provisions of the National Bank Act which are designed to insure a ratable distribution of assets among creditors. *The same reasoning would forbid the creation of a lien on assets as security for funds collected. And, of course, if the creation of such a lien be beyond the powers of the bank, it could not be created by act of the state legislature; for the legislature could not provide that action on the part of the bank should give rise to a lien which the bank, by reason of the limitations imposed upon it by act of Congress, was powerless to create.*" (Italics inserted)

In the instant case as well as in the North Carolina case the trust claimant places much reliance on the opinion of this court in Lewis v. Fidelity and Deposit Company, *supra*. But, as Judge Parker states in his opinion in Royal Manufacturing Company v. Spradlin, *supra*:

> "*The case of Lewis v. Fidelity & Deposit Co., 292 U. S. 559, relied upon by appellee, is in reality an authority against its position.* In that case a statute of Georgia, creating a general lien on the assets of banks as security for deposits of state funds, was held to have application to a national bank merely because the act of Congress of June 25, 1930, c. 604, 46 Stat. 809, 12 U. S. C. A. 90, authorized a national bank to give security for a deposit of public funds of the same kind as authorized by state law for state banking institutions. *The Supreme Court said that no lien under the Georgia statute arose in 1928 when the deposit was made, and that the judgment of the court below sustaining the lien would have been reversed but for the enactment by Congress of the act of 1930. See p. 564. Here there is no act of Congress authorizing the creation of a lien on the assets of a national bank as security for collections; and the act of the North Carolina legislature can no more create a lien on the assets of a national bank than could the Georgia statute without the aid of the act of 1930.*" (Italics inserted)

In a number of cases trust claimants against insolvent banks have urged courts of equity to resort to fictions concerning segregation, but the Federal Courts have consistently declined to accept such suggestions even where the bank had a duty to segregate, which does not appear in the instant case. To quote from the summary of an article by Mr. Justice Stone entitled "Legal Problems in the Transmission of Funds", Columbia Law Review, June 1921, page 525:

> "The very essence of the right of priority over other creditors depends upon the setting apart of a particular fund for the benefit of the depositor. There is no

basis for giving one depositor a priority over another unless this is an essential part of the transaction. It is, of course, important that bankers should be held to a high standard of accountability to their customers. It would seem, however, that this should be accomplished by appropriate legislation which should inure to the benefit of depositors generally *rather than by the adoption of a rule of law creating special rights in favor of a limited class of customers on the theory that they are the beneficiaries of a quasi-trust fund which never in fact exists or is intended to exist as such.*" (Italics inserted)

On page 518 of the article Mr. Justice Stone says:

"The doctrine that money deposited with a bank for a special purpose is a fiduciary deposit, has been carried to extreme lengths in this country *in those cases where no specific money was ever paid to the bank, the customer merely giving or procuring a credit in account in favor of the bank* upon the banker's undertaking to effect payment at a distant point. Here there is no specific deposit. *The transaction results only in a credit appearing on the books of the bank, there being at no point of time any specific money or other res paid to or set apart or held by the bank for account of the customer. Even if there were an executory undertaking of the bank to become a fiduciary by setting apart such specific sum, such a relationship is not established until there is some actual setting apart or segregation of the money or some other res as the subject matter of the fiduciary relationship.*" (Italics inserted)

In the case of Schumacher v. Brinson, 52 Fed. (2nd) 821, the Circuit Court of Appeals for the Fourth Circuit resorted to a fiction but its decision allowing a trust claim was unanimously reversed by this court as Blakey v. Brinson, 286 U. S. 254, this court stating, pages 262, 263:

"The court below thought that the legal consequence to be attributed to the debiting of the account with the supposed purchase price of the bonds was the same as if the respondent had cashed a check for the amount

and had then proceeded to hand the money back to the bank under a specific agreement between him and the bank that the money was to be held as a special fund, for the sole purpose of completing the purchase. This view is not without support. (Citing authorities.) Such a procedure, *if actually carried out*, might afford a basis which is lacking here, for the inference that respondent, no longer content with the role of creditor, had sought to establish a trust fund. But *the mere debiting of his account, without more, for the reimbursement of the bank for the obligation which it was supposed to have incurred or paid, lends no support to such an inference. The cancellation of the credit balance by the debit neither suggests any intention to establish a trust nor points to any identifiable thing which could be the subject of it.*" (Italics inserted)

The following excerpts indicate similar action by other courts. Smith v. Zemurray, (C. C. A. 5) 69 Fed. (2nd) 5, 6:

"To the appellee's 'as if' argument, 'the matter is to be treated as though Robinson had presented the check to the teller and on receiving the money had paid it back over the counter to buy a draft,' American National Bank v. Miller, 229 U. S. 520, 33 S. Ct. 883, 57 L. Ed. 1310,' the receiver replies: 'Not so. We know from Robinson's own testimony that this did not occur. We know from it that what did occur was an exchange of the paper of a bank, hopelessly insolvent, if plaintiff is right, in the form of an accepted draft on it, for paper of the same bank in the form of its draft on New York. This and nothing more.' He argues, too, that *when what actually occurred is known, it is idle to speculate on what might have been the legal effect of an entirely different occurrence.* Blakey v. Brinson, 286 U. S. 254, 52 S. Ct. 516, 76 L. Ed. 1089, 82 A. L. R. 1288." (Italics inserted)

Wisdom v. Keen, (C. C. A. 5) 69 Fed. (2nd) 349, 350:

"This, then, is a case in which the bank and its customer definitely agreed that $1,200.00 in cash should be

held by the bank in escrow, to be delivered (not paid) on a condition and checks were given to the bank on which it was to get the cash out of its own vault. The obligation was perfect to segregate and hold the cash. *Equity if dealing with the bank alone might well consider that it had done what it should have done and might well hold it to the consequences.* American National Bank v. Miller, 229 U. S. 517, 33 S. Ct. 883, 57 L. Ed. 1310. *But in dealing with the distribution of the assets of an insolvent national bank and with the requirement of ratable dividends to all claimants a more stringent adherence to what was actually done is proper.* Here the bank agreed to segregate a trust res but never did it. By their mutual intent the bank's relation to Keen was that of a trustee rather than a debtor, but there is still no identifiable trust res traceable as such, but only a liability for a breach of trust in failing to create the res. This liability, absent a statutory priority or lien, has no higher dignity than other general liabilities. As to every general creditor the bank has failed to do what it ought to have done and what it promised to do. The federal statute puts all such claimants on an equality. Even claims due the United States have no preference. Cook County National Bank v. United States, 107 U. S. 445, 2 S. Ct. 561, 27 L. Ed. 537." (Italics inserted)

Hecker-Jones-Jewell Milling Co. v. Cosmopolitan Trust Co. (Supreme Judicial Court of Massachusetts) (De Courcy, J.) 136 N. E. 333-335:

"The other theory is that the transaction by which the draft was paid was in legal effect the same as if B. Greenglass & Son had drawn from their account through the paying teller the sum of $3,518.00, in money, and then handed it back to the collecting teller in payment of the draft. *But that is not what the debtor did; and the difference is essential, not a mere matter of form. The payment made to the bank was not cash,* to which the moment before it had not the slightest claim, and which therefore would count as wholly separate 'proceeds' of the collection; *it was*

> *merely the lessening of one of its own debts, and productive of nothing even remotely suggesting a 'res' for a trust. The difference between the legal significance of the actual and the assumed courses of action cannot be ignored or confused.*" (Italics inserted)

People v. Merchants & Mechanics Bank, 78 N. Y. 269:

> "The learned counsel contends that the Troy Bank was agent of the Chemical Bank to receive payment of the check. Suppose it were, *what did it receive as such payment? Simply its own obligation. If anything was set apart by charging up the check, it was only so much of the bank's indebtedness to its depositor.* * * * To make this case analogous it would be necessary to show that the Troy Bank had separated from its general assets, and placed in the hands of some depositary, a sum sufficient to pay the check, for the express purpose of being so applied, and that this fund had come to the hands of the receiver in some form. There is no approach in this case to any such state of facts." (Italics inserted)

The only Federal decision we find wherein a fiction was resorted to in allowing a trust claim against the Receiver of an insolvent National bank is that of Schumacher v. Harriett, 52 Fed. (2nd) 817 which may possibly be relied on by the respondent. The error of this decision as we see it is discussed in detail in the petitioner's brief in the companion case of Adams v. Champion, No. 374, this term. The arguments against the soundness of the Harriett decision are summarized in the recent opinions of the Circuit Court of Appeals for the Fifth Circuit as follows:

Pottorff v. Key, 67 Fed. (2nd) 833, 834:

> "Schumacher v. Harriett (C. C. A.) 52 Fed. (2nd) 817, 82 A. L. R. 1, is much relied on to sustain the judgment appealed for. The court there reviews the cases and concedes that they establish such principles as we have just asserted, but avoids their consequences *by the novel view* that a trust check, when treated by a bank

as one of its cash items, is thereby confused with its cash as though it had been unidentifiable currency; and that, if the bank misuses the check, it thereby sets apart as a trust res an equivalent value of other cash assets. *Such a doctrine amounts to saying that in every case of misapplied money or money's equivalent the wrongdoer's other cash and cash items stand in its place so long as he has any, establishing in effect a general lien on all such.* 'If the plaintiff's contention be well founded, and to follow misappropriated moneys it is only necessary to show that a receiver has, and that the trustee had, assets, the rule is simply that a demand for such moneys is a preferred claim against any substantial estate. *To adopt this view is to do away with all the equitable principles out of which the right to follow trust funds grew.*' American Can Co. v. Williams (C. C. A.) 178 F. 420, at page 423. *We hold in this connection that, if a trust res can be followed, it must be; and that a lien by confusion can be fixed on a fund only when the confusion is actual and when the fund is shown to have really received and to still contain the trust res or its proceeds.* The judgment is reversed, with direction to disallow appellee's claim as preferred and to allow it as a general claim only." (Italics inserted)

Wisdom v. Keen, 69 Fed. (2nd) 349, 350:

"The view that when a bank becomes obligated to collect for another person checks drawn on itself and makes entries of their collection, it must in equity be considered to have done what it should have done, to wit, to have collected them in cash though afterwards commingling the customer's cash thus collected with its own, so that a traceable res is brought into being with title vested in the customer, has been adopted by a growing number of State courts and is said to be the majority view in an elaborate examination of the cases in 82 A. L. R. page 97. *It was pressed to its furtherest etxent in the Fourth Circuit in Schumacher v. Harriett,* 52 Fed. (2nd) 817, 82 A. L. R. 1, *and Schumacher v. Brinson,* 52 Fed. (2nd) 821. *Otherwise the Federal cases have been to the contrary,* 82 A. L. R. 101. Schu-

macher v. Brinson was appealed and reversed as Blakey v. Brinson, 286 U. S. 254, 52 S. Ct. 516, 76 L. Ed. 1089, 82 A. L. R. 1288. *We refused to follow Schumacher v. Harriett in Pottorff v. Key* (C. C. A.), 67 Fed (2nd) 833. At the conclusion of the opinion in *Texas & Pacific R. Co. v. Pottorff*, 54 S. Ct. 416, 78 L. Ed. ...., *the Supreme Court again indicates the necessity of an identifiable trust res in order to create a trust by misconduct as distinguished from a general liability in contract or tort. Whether the question be one of general equity jurisprudence or of the application of the federal law relating to insolvent national banks, the views of the Federal courts must in such courts be controlling.*" (Italics inserted)

When Circuit Judge Parker, the author of the Harriett opinion, was urged to resort to a similar fiction to establish a trust claim against an insolvent National bank while sitting as a District Judge in First National Bank of Ventura v. Williams, 15 Fed. (2nd) 585, 588, he said:

> "The answer to this is that courts must decide cases, not upon suppositions, but upon facts as proven or admitted, and the admitted fact is that cash was not received for the check, but that it was used merely to reduce the liabilities of the bank."

Of course had the collecting National Bank segregated a part of its cash or cash items and earmarked the same, the trust claim contended for could be established. The difference between segregation and non-segregation is illustrated in St. Augustine Paint Company v. McNair (C. C. A. 5) 59 Fed. (2) 755, where the bank physically segregated a part of its cash to purchase the claimant's check held for collection. The court in its opinion at page 757 said:

> "The conversion of the check into cash and segregation of such cash from the bank's general assets before using the check are of vital consequence, as those facts distinguish that transaction from those in which a bank of deposit merely credited a check to the depositor's account so as to become the depositor's debtor, and

thereafter used the check to pay the bank's own debts in such a manner that the proceeds were absorbed in a clearing transaction with no gain to the receiver, such as in Empire State Surety Co. v. Carroll Co. (C. C. A. 8) 194 Fed. 593, and other cases cited." (Italics inserted)

The respondent has filed a supplemental brief wherein it designates certain statements in the brief of the Comptroller of the Currency as amicus curiae as "erroneous" or "incorrect". It is submitted that all statements contained in the amicus curiae brief are amply supported by the authorities cited therein and in this brief. Nothing contained in the Comptroller's brief is withdrawn or modified except the statement that this case turns on the tracing of funds feature. The claim in the instant case is general only because of complete inability to trace any proceeds to the Receiver. No res exists and consequently there is no trust relationship. Accordingly as in Blakey v. Brinson, *supra*, it should not be necessary to consider the tracing of funds questions.

The national banking laws, and related Acts, together with a long line of decisions by this Court, clearly evidence an intent to safeguard the assets of insolvent National banks, in liquidation, thus insuring a maximum distribution to the depositors and creditors. Taxes due the United States which would be paid from the funds of depositors are abated. (Sec. 570, Title 12 U. S. C. A.) The preference given the United States as a sovereign against insolvent estates generally is inapplicable to such banks. Suits to wind up the affairs of such banks are made cognizable in the Federal courts, *independent of the amount involved.* A separate system of liquidation is provided, independent of the Bankruptcy Act. Sales and compromises of assets can be made only after court approval and advances to protect assets can be made only upon approval by the Secretary of the Treasury. Annual reports of the results of liquidation are required to be made to Congress. While

the claimants in the instant case (and in the companion cases Nos. 340 and 374) assert ownership of property taken over by the Receivers they are in fact, as established by the record, seeking to be made whole from the funds of the depositors. To permit any class of claimants to be paid in full from the funds of depositors, when such funds were in no way enriched by the claimants' transactions, would flagrantly violate the principles heretofore adhered to in liquidating insolvent National banks.

The depositors and other creditors of this insolvent National bank—the beneficial owners of all its assets—will suffer a very substantial loss because of their dealings with the bank. The equities of these depositors and other creditors are at least equal to those of the respondent. The record establishes that no part of the assets that passed to the Receiver came into the bank as a result of the respondent's transaction. All of the assets that passed to the Receiver came into the bank as the result of transactions other than the respondent's. None of the assets of the bank were segregated to respond for the respondent's claim under the provisions of the Bank Collection Code and no segregation was intended by that statute. Section 13 of the Bank Collection Code is inapplicable to insolvent National banks. Under these circumstances the court below should have found for the bank Receiver and classified the respondent's claim as general only.

(C) The jurisdiction of the District Court is limited to the determination of the validity of the trust claim asserted, and to a direction to the Receiver to certify the claim to the Comptroller of the Currency for payment in due course of administration. The court below should have reversed the District Court's order to the Receiver to pay forthwith; should have dissolved the permanent injunction issued by the District Court restraining the Receiver from disposing of the bank's assets as required by the National Bank Act, and should have allowed a general claim.

The court below should have reversed the District Court's order to the Receiver to pay a sum of money forthwith and should have dissolved the permanent injunction issued by the District Court restraining the Receiver from disposing of the bank's assets as required by the National Bank Act.

It is the position of the bank Receiver that all that is said in the following excerpts from opinions by this court concerning the lack of authority of State courts to in any way control the assets of a National bank being liquidated through a Receiver appointed by the Comptroller of the Currency is equally applicable to the Federal courts:

Earle v. Pennsylvania, 178 U. S. 449, 454:

> "We must not, however, be understood as holding that the distribution of the bank's assets in the hands of the receiver could have been in anywise directly controlled by the state court or seized under an attachment or execution in the hands of any state officer. On the contrary, the direction in the statute that the receiver pay over all moneys realized by him from the assets of the bank to the Treasurer of the United States, subject to the order of the Comptroller, furnished a rule of conduct for him which neither an order of nor any proceedings in the state court could affect, modify or change. The scheme of the statute relating to suspended national banks is that from the time of a bank's suspension all its assets, of whatever kind, as they are at the time of suspension, pass in the first instance, to the receiver, the proceeds thereof to be distributed by the Comptroller among those whose claims are proved to his satisfaction or are adjudicated by some court of competent jurisdiction. So when the Chestnut Street National Bank suspended and went into the hands of a receiver the entire control and administration of its assets were committed to the receiver and the Comptroller, subject, however, to any rights of priority previously acquired by the plaintiff through the proceedings in the suit against Long."

Earle v. Conway, 178 U. S. 456, 457:

> "No sound reason can be given why the receiver of a National bank may not be notified by service upon him of an attachment issued from a state court of the nature and extent of the interest asserted or sought to be acquired by the plaintiff in the attachment in the assets in his custody. But for the reasons stated in Earle v. Pennsylvania, such an attachment cannot create any lien upon specific assets of the bank in the hands of the receiver, nor disturb his custody of those assets, nor prevent him from paying to the Treasurer of the United States, subject to the order of the Comptroller of the Currency, all moneys coming to his hands or realized by him as receiver from the sale of the property and assets of the bank. After the service of the attachment upon the receiver it became the duty of the latter to hold any funds coming to his hands through the Treasurer of the United States as the proceeds of the sale of the bank's assets subject to any interest which the plaintiff may have legally acquired therein as against his debtor under the attachment issued on the judgment in his favor in the state court."

In the instant case the respondent does not seek the return of specific property it claims to own but seeks to impress a trust on the cash and cash items of the collecting National bank because of an alleged commingling of its property. Under the provisions of Section 194, Title 12, U. S. C. A., claims against the bank's cash and cash items may be proved to the satisfaction of the Comptroller or determined in a court of competent jurisdiction. In distributing the proceeds of property that comes into his hands as apparent assets of an insolvent National bank, the Comptroller always endeavors to take cognizance and give full effect to the final decisions of Federal or State courts involving claims against such bank. If the trial court had jurisdiction to direct payments forthwith from the bank's cash and cash items or enjoin the disposition of the same it could direct the payment of the entire amount thereof to one claimant. Other claimants who may have proved trust

claims against the cash and cash items to the satisfaction of the Comptroller, as permitted by the statute, would thus be denied payment as contemplated by the Act. Only where claims found valid by the courts are directed to be certified to the Comptroller of the Currency for payment in due course of administration can the rights of all concerned be protected, because the bank's assets, including all apparent assets, are in the hands of the Comptroller for distribution. The cash that passed to the Receiver of the collecting National bank and the proceeds of the cash items that passed into his hands had been transferred to the Comptroller of the Currency prior to the issuance of the trial court's injunction, and consequently the injunction would have to issue against the Comptroller of the Currency, who was not within the jurisdiction of the court.

The trial court's direction to the Receiver to pay forthwith might result in the Receiver being held in contempt for not paying over moneys which are not within his control. In this connection the Circuit Court of Appeals for the Fifth Circuit in Richardson v. Louisville Banking Company, 94 Fed. 442, 449, said:

> "An objection is made to the form of the decree rendered in the court below, in that it commands the receiver to pay over to the complainant a certain large sum of money within 10 days, when, as a matter of fact, and in accordance with law, the receiver is not in personal custody of the funds in question, but the same are in the hands of the comptroller of the currency. The effect of the decree, as rendered, might be that the receiver would be in contempt for not paying over moneys which are not within his control. See Merrill v. Bank, 41 U. S. App. 529, 21 C. C. A. 282, and 75 Fed. 148."

In Merrill v. First National Bank of Jacksonville (C. C. A. 5), 75 Fed. 148, 153, the court, in its opinion, said:

> "In general, the receiver of a National bank has been held to be a mere instrument of the Comptroller, and

subject in all respects to his instruction. Kennedy v. Gibson, 8 Wall. 498; Bank v. Kennedy, 17 Wall. 21. In Eastern Townships Bank v. Vermont National Bank, 22 Fed. 186, the proper form of a decree in a case similar to the one in hand was considered in reference to section 5236, Rev. St., and Case v. Bank, 100 U. S. 446. It was held that judgments in such cases should be certified by the receiver through the Comptroller, and be paid in due course of administration. In Case v. Bank, *supra,* the judgment was, after reciting the amount of the demand, etc., as follows:

> 'That Frank F. Case, receiver, do recognize the said Citizens Bank of Louisiana as creditor, * * * and that he do pay the same or certify the same to the Comptroller, to be paid in due course of administration; * * * and that the Citizens Bank of Louisiana do receive, before further payment to creditors, its due proportion of dividends pro rata with those already paid to the creditors of the Crescent City National Bank.'

"In this case it does not appear that the form of the judgment was contested, but in affirming the judgment the court did say:

> 'Beyond all doubt, the validity of their debt is established by the verdict and judgment; and, if so, it requires neither argument nor authorities to show that the order given by the circuit court to provide for the payment of the amount recovered was proper and correct.' Id. 456."

This injunction question was considered by the Circuit Court of Appeals of the Second Circuit in American Can Co. v. Williams, 149 Fed. 200, affirmed 153 Fed. 882, where the right to enjoin was sustained in a divided opinion. The bank Receiver submits, however, in view of the fact that the Comptroller of the Currency alone can do justice to all parties, that the law is correctly stated in the following dissenting opinion of Judge Townsend (149 Fed. 200):

> "I dissent from the opinion of the majority of the court. The order in question enjoins the receiver 'from

disposing in any manner of any funds in his hands as receiver of the Fredonia National Bank by transmission to the Treasurer of the United States or otherwise, so as to reduce' the amount claimed by the plaintiff as a preference in the pending suit.

"The Federal statute makes it the duty of the defendant to take possession of the assets of the insolvent institution, and to pay over all moneys resulting therefrom to the Treasurer of the United States, subject to the order of the Comptroller. There is no evidence that the defendant is doing or threatens to do any act in violation of the plaintiff's right. It would seem from the language of section 5236 of the Revised Statutes (U. S. Comp. St. 1901, p. 3508) that the comptroller and not the defendant, would be the proper person to pay the plaintiff's claim if it were finally sustained. In the absence of evidence that unless the injunction issue there will be an invasion of the plaintiff's rights, there is no sufficient justification therefor. The right to a preliminary injunction is not granted ex debito justitiae, but the application is addressed to the sound discretion of the court. The discretion is not an arbitrary one, but is to be exercised subject to the established principles of law. High on Injunctions, Sec. 11, 13.

"*It is to be assumed that the receiver, the Treasurer and the Comptroller will execute their duties according to law.* I am of the opinion therefore, that no adequate ground has been shown to justify the interference by injunction with the executive officers of the Government in the discharge of their duties in accordance with the statute." (Italics inserted.)

This dissenting opinion seems to be fortified by the following excerpt from the very recent decision of the Circuit Court of Appeals, Fifth Circuit in Taylor v. Spurway, et al., 72 Fed. (2nd) 97. 99:

"It is contended by the appellee that he has no fund in his custody as it is the duty of a receiver of a national bank to cover all moneys coming into his hands in liquidation of the bank's affairs into the treasury, subject to the order of the Comptroller who alone has

power to declare dividends. While this is true, the receiver is required to conduct his affairs with honesty and fair dealing, and a suit will lie against him to determine the rights of parties claiming a lien on assets in his hands. Merrill v. National Bank of Jacksonville, 173 U. S. 131, 19 S. Ct. 360, 43 L. Ed. 640. If it should transpire that the receiver has no funds to respond to a judgment, *it must be assumed that the Comptroller, although beyond the reach of process of the court rendering the judgment, will give effect to a valid judgment of a court of competent jurisdiction.* Earle v. Pennsylvania, 178 U. S. 449, 20 S. Ct. 915, 44 L. Ed. 1146. We are not aware of any case in which the receiver of a national bank has been enjoined from disposing of funds in his custody, but he is not above the law and, if he be guilty of such gross fraud as alleged, a court of equity undoubtedly would have authority to do so." (Italics inserted.)

The bank Receiver submits that even though the respondent's claim shall be classified as general only, consideration should be given by this Court to the propriety of the District Court's issuance of a permanent injunction and order to pay forthwith, because the bank Receiver has been restrained since September 13, 1933, from disposing of a part of the bank's assets in the manner prescribed by the National Bank Act.

VII.

CONCLUSION.

It is believed that the foregoing discussion establishes that no trust arose in the present case; that the assets of the collecting National Bank were not augmented by the collection of the respondent's check; that no trust res can be traced to the assets acquired by the bank Receiver; that the dignity of the respondent's claim is in no way increased by any of the provisions of the Bank Collection Code; that the court below should have reversed the trial court's direction to the Receiver to pay forthwith and should have dis-

solved the injunction issued by the trial court; and that an affirmance may be construed to mean the overruling of the great body of Federal decisions requiring the existence of a trust res and the tracing of the same to the Receiver or that a State statute in conflict with the National Bank Act can be made applicable in the liquidation of an insolvent National bank.

It is submitted that the decision of the court below should be reversed.

Respectfully submitted,

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APPENDIX.

U. S. C. A. Title 12, Sec. 194.

DIVIDENDS ON ADJUSTED CLAIM; DISTRIBUTION OF ASSETS. From time to time, after full provision has been first made for refunding to the United States any deficiency in redeeming the notes of such association, the Comptroller shall make a ratable dividend of the money so paid over to him by such receiver on all such claims as may have been proved to his satisfaction or adjudicated in a court of competent jurisdiction, and, as the proceeds of the assets of such association are paid over to him, shall make further dividends on all claims previously proved or adjudicated; and the remainder of the proceeds, if any, shall be paid over to the shareholders of such association, or their legal representatives, in proportion to the stock by them respectively held. (R. S. Sec. 5236)

PROGRAM OF STATE LEGISLATION 1929—PART 2.

Recommended by the
AMERICAN BANKERS ASSOCIATION

BANK COLLECTION CODE.

Draft prepared jointly by Thomas B. Paton and Thomas B. Paton, Jr., General Counsel and Assistant General Counsel, American Bankers Association, with explanatory notes, and designed for uniform enactment in all the states.

Issued under the auspices of the Committee on State Legislation,
AMERICAN BANKERS ASSOCIATION

FOREWORD.

There has long been need for a uniform code of rules governing bank collections which will give the sanction of law to modern customs and practices of banks and obviate the necessity for the printing of special agreements on deposit slips, pass books and other literature for their protection. Not only are existing rules growing out of earlier conditions which no longer obtain, unsuited to present conditions, but the conflict of such rules, as established in the different states, makes uniformity a desideratum especially as the currency of checks and other paper is nation-wide in scope and the rules governing the collection and payment of such paper should be uniform, irrespective of state lines.

To accomplish the purpose of uniformity and modernization of the law governing bank collections, three successive tentative drafts of a bank collection code have been prepared and submitted to various bankers, expert in the practice of check collection, to attorneys for banks and to mem-

bers of the Committee on State Legislation and the State Legislative Council of the American Bankers Association for their suggestions and criticism.

The third tentative draft was approved in substance at the meeting on October 1, 1928, of the Committee on State Legislation subject to technical changes which the General Counsel was authorized to make preliminary to its being urged by the Committee on State Legislation through state bankers associations for enactment by the legislatures of the different states and this action was approved by the Executive Council at that time.

As finally drafted, the code is now presented to the members of the State Legislative Committee and the State Legislative Council in the various states and to Secretaries of the state bankers associations for their consideration and approval of the appropriate committees of such state associations preparatory to being urged through their associations at the 1929 and subsequent sessions of the state legislatures.

It is hoped the detailed provisions herein will prove to be practicable and can be uniformly enacted although the draft still must be regarded, in a measure, as tentative rather than a completed draft. Due to the complications of the subject it is a difficult one to regulate with scientific exactness. Attention is particularly invited to the provision that is contained in Section 11 which continues the liability of the maker and prior parties upon a check presented by mail to a drawee which defaults in payment. Montana has already adopted such principle of liability as part of its legislation, the theory being that a depositor who tenders his check which requires mailing for payment, should not escape liability to his creditor where the bank which he has designated to make payment cannot make good. It will be noted that this section merely gives an option to the holder to dishonor his check and preserve his liability; the option need or need not be exercised. If not exercised, then the drawer of the check is dicharged if the drawee charges it to his account but in such case there arises a preference in the assets of the insolvent bank in favor of the owner.

BANK COLLECTION CODE

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AN ACT TO EXPEDITE AND SIMPLIFY THE COLLECTION AND PAYMENT BY BANKS OF CHECKS AND OTHER INSTRUMENTS FOR THE PAYMENT OF MONEY.

Be it enacted

SECTION 1. [Definitions.] For the purposes of this code:

(A) Bank. The term "bank" shall include any person, firm or corporation engaged in the business of receiving and paying deposits of money within this state. A branch or office of any such bank shall be deemed a bank for the purpose of this act.

(B) Item. The term "item" means any check, note or other instrument providing for the payment of money.

SECTION 2. [Bank Is Agent for Collection.]

Except as otherwise provided by agreement and except as to subsequent holders of a negotiable instrument payable to bearer or indorsed specially or in blank, whether an item is deposited or received for collection, the bank of deposit shall be agent of the depositor for its collection and each subsequent collecting bank shall be sub-agent of the depositor but shall be authorized to follow the instructions of its immediate forwarding bank and any credit given by any such agent or sub-agent bank therefor shall be revocable until such time as the proceeds are received in actual money or an unconditional credit given on the books of another bank, which such agent has requested or accepted. Where any such bank allows any revocable credit for an item to be withdrawn, such agency relation shall nevertheless continue except the bank shall have all the rights of an owner thereof against prior and subsequent parties to the extent of the amount withdrawn.

SECTION 3. [Item on Same Bank.]

A credit given by a bank for an item drawn on or payable at such bank shall be provisional, subject to revocation at or before the end of the day on which the item is deposited in the event the item is found not payable for any reason. Whenever a credit is given for an item deposited after banking hours such right of revocation may be exercised during the following business day.

SECTION 4. [Legal Effect of Indorsements.]

An indorsement of an item by the payee or other depositor "for deposit" shall be deemed a restrictive indorse-

ment and indicate that the indorsee bank is an agent for collection and not owner of the item.

An indorsement "pay any bank or banker" or having equivalent words shall be deemed a restrictive indorsement and shall indicate the creation of an agency relation in any subsequent bank to whom the paper is forwarded unless coupled with words indicating the creation of a trustee relationship; and such indorsement or other restrictive indorsement whether creating an agency or trustee relationship shall constitute a guaranty by the indorser to all subsequent holders and to the drawee or payor of the genuineness of and the authority to make prior indorsements and also to save the drawee or payor harmless in the event any prior indorsement appearing thereon is defective or irregular in any respect unless such indorsement is coupled with appropriate words disclaiming such liability as guarantor.

Where a deposited item is payable to bearer or indorsed by the depositor in blank or by special indorsement, the fact that such item is so payable or indorsed shall not change the relation of agent of the bank of deposit to the depositor, but subsequent holders shall have the right to rely on the presumption that the bank of deposit is the owner of the item. The indorsement of an item by the bank of deposit or by any subsequent holder in blank or by special indorsement or its delivery when payable to bearer, shall carry the presumption that the indorsee or transferee is owner provided there is nothing upon the face of the paper or in any prior indorsement to indicate an agency or trustee relation of any prior party. But where an item is deposited or is received for collection indorsed specially or in blank, the bank may convert such an indorsement into a restrictive indorsement by writing over the signature of the indorser the words "for deposit" or "for collection," or other restrictive words to negative the presumption that such bank of deposit or indorsee bank is owner; and in the case of an item deposited or received for collection payable to bearer, may negative such presumption by indorsing thereon the words "received for deposit" or "received for collection" or words of like import.

SECTION 5. [Duty and Responsibility of Bank Collecting Agents.]

It shall be the duty of the initial or any subsequent agent collecting bank to exercise ordinary care in the collection of

an item and when such duty is performed such agent bank shall not be responsible if for any cause payment is not received in money or an unconditional credit given on the books of another bank, which such agent bank has requested or accepted. An initial or subsequent agent collecting bank shall be liable for its own lack of exercise of ordinary care but shall not be liable for the neglect, misconduct, mistakes or defaults of any other agent bank or of the drawee or payor bank.

SECTION 6. [Rules of Ordinary Care in Forwarding and Presentment.]

(A) Where an item is received on deposit or by a subsequent agent bank for collection, payable in another town or city, it shall be deemed the exercise of ordinary care to forward such item by mail, not later than the business day next following its receipt either (1) direct to the drawee or payor in the event such drawee or payor is a bank or (2) to another bank collecting agent according to the usual banking custom, either located in the town or city where the item is payable or in another town or city.

(B) Where an item is received on deposit or by a subsequent agent bank for collection, payable by or at another bank in the same town or city in which such agent bank is located, it shall be deemed the exercise of ordinary care to present the item for payment at any time not later than the next business day following the day on which the item is received either (1) at the counter of the drawee or payor by agent or messenger or (2) through the local clearing house under the regular established procedure, or according to the usual banking custom where the collecting or payor bank is located in an outlying district.

(C) The designation of the above methods shall not exclude any other method of forwarding or presentment which under existing rules of law would constitute ordinary care.

SECTION 7. [Items Received Through the Mail.]

Where the item is received by mail by a solvent drawee or payor bank, it shall be deemed paid when the amount is finally charged to the account of the maker or drawer.

SECTION 8. [Items Lost in Transit.]

Where an agent bank forwards an item for collection, it shall not be responsible for its loss or destruction in transit or, when in the possession of others, for its inability to

repossess itself thereof, provided there has been no lack of ordinary care on its part.

SECTION 9. [Medium of Payment.]

Where ordinary care is exercised, any agent collecting bank may receive in payment of an item without becoming responsible as debtor therefor, whether presented by mail, through the clearing house or over the counter of the drawee or payor, in lieu of money, either (a) the check or draft of the drawee or payor upon another bank or (b) the check or draft of any other bank upon any bank other than the drawee or payor of the item or (c) such method of settlement as may be customary in a local clearing house or between clearing banks or otherwise: provided that whenever such agent collecting bank shall request or accept in payment an unconditional credit which has been given to it on the books of the drawee or payor or on the books of any other bank, such agent collecting bank shall become debtor for such item and shall be responsible therefor as if the proceeds were actually received by it in money.

SECTION 10. [Medium of Remittance.]

Where ordinary care is exercised, any agent collecting bank may receive from any subsequent bank in the chain of collection in remittance for an item which has been paid, in lieu of money, the check or draft of the remitting bank upon any bank other than itself or the drawee or payor of the item or such other method of settlement as may be customary: provided that whenever such agent collecting bank shall request or accept an unconditional credit which has been given to it on the books of the remitting bank or on the books of any other bank, such agent collecting bank shall become debtor for such item and shall be responsible therefor as if the proceeds were actually received by it in money.

SECTION 11. [Election to Treat as Dishonored Items Presented by Mail.]

Where an item is duly presented by mail to the drawee or payor, whether or not the same has been charged to the account of the maker or drawer thereof or returned to such maker or drawer, the agent collecting bank so presenting may, at its election, exercised with reasonable diligence, treat such item as dishonored by non-payment and

recourse may be had upon prior parties thereto in any of the following cases:

(1) Where the check or draft of the drawee or payor bank upon another bank received in payment therefor shall not be paid in due course;
(2) Where the drawee or payor bank shall without request or authority tender as payment its own check or draft upon itself or other instrument upon which it is primarily liable;
(3) Where the drawee or payor bank shall give an unrequested or unauthorized credit therefor on its books or the books of another bank; or
(4) Where the drawee or payee shall retain such item without remitting therefor on the day of receipt or on the day of maturity if payable otherwise than on demand and received by it prior to or on such day of maturity.

Provided, however, that in any case where the drawee or payor bank shall return any such item unpaid not later than the day of receipt or of maturity as aforesaid in the exercise of its right to make payment only at its own counter, such item cannot be treated as dishonored by nonpayment and the delay caused thereby shall not relieve prior parties from liability.

Provided further that no agent collecting bank shall be liable to the owner of an item where, in the exercise of ordinary care in the interest of such owner, it makes or does not make the election above provided or takes such steps as it may deem necessary in cases (2), (3) and (4) above.

SECTION 12. [Notice of Dishonor of Items Presented by Mail.]

In case of the dishonor of an item duly presented by mail as provided for in the next preceding section, notice of dishonor of such item to prior parties shall be sufficient if given with reasonable diligence after such dishonor; and further in the event of failure to obtain the return of any such item notice of dishonor may be given upon a copy of written particulars thereof, and delay in giving notice of dishonor caused by an attempt with reasonable diligence to obtain return of such item shall be excused.

SECTION 13. [Insolvency and Preferences.]

1. When the drawee or payor, or any other agent collecting bank shall fail or be closed for business by (official to be designated) or by action of the board of directors or by other proper legal action, after an item shall be mailed or otherwise entrusted to it for collection or payment but before the actual collection or payment thereof, it shall be the duty of the receiver or other official in charge of its assets to return such item, if same is in his possession, to the forwarding or presenting bank with reasonable diligence.

2. Except in cases where an item or items is treated as dishonored by non-payment as provided in Section 11, when a drawee or payor bank has presented to it for payment an item or items drawn upon or payable by or at such bank and at the time has on deposit to the credit of the maker or drawer an amount equal to such item or items and such drawee or payor shall fail or close for business as above, after having charged such item or items to the account of the maker or drawer thereof or otherwise discharged his liability thereon but without such item or items having been paid or settled for by the drawee or payor either in money or by an unconditional credit given on its books or on the books of any other bank, which has been requested or accepted so as to constitute such drawee or payor or other bank debtor therefor, the assets of such drawee or payor shall be impressed with a trust in favor of the owner or owners of such item or items for the amount thereof, or for the balance payable upon a number of items which have been exchanged, and such owner or owners shall be entitled to a preferred claim upon such assets, irrespective of whether the fund representing such item or items can be traced and identified as part of such assets or has been intermingled with or converted into other assets of such failed bank.

3. Where an agent collecting bank other than the drawee or payor shall fail or be closed for business as above, after having received in any form the proceeds of an item or items entrusted to it for collection, but without such item or items having been paid or remitted for by it either in money or by an unconditional credit given on its books or on the books of any other bank which has been requested or accepted so as to constitute such failed collecting or other bank debtor therefor, the assets of such agent collecting

bank which has failed or been closed for business as above shall be impressed with a trust in favor of the owner or owners of such item or items for the amount of such proceeds and such owner or owners shall be entitled to a preferred claim upon such assets, irrespective of whether the fund representing such item or items can be traced and identified as part of such assets or has been intermingled with or converted into other assets of such failed bank.

SECTION 14. [Act not Retroactive.]

The provisions of this act shall not apply to transactions taking place prior to the time when it takes effect.

SECTION 15. [Cases not Provided for in Act.]

In any case not provided for in this act the rules of law and equity, including the law merchant and those rules of law and equity relating to trusts, agency, negotiable instruments and banking, shall continue to apply.

SECTION 16. [Uniformity of Interpretation.]

This act shall be so interpreted and construed as to effectuate its general purpose to make uniform the law of those states which enact it.

SECTION 17. [Short Title.]

This act may be cited as the bank collection code.

SECTION 18. [Inconsistent Laws Repealed.]

All acts or parts of acts inconsistent with this act are hereby repealed.

SECTION 19. [Time of Taking Effect.]

This act shall take effect [ ].

EXPLANATORY NOTES

SECTION 1. [Definitions.]

The definition of the term "bank" is broad enough to include all banks whether organized under State or Federal laws. The definition also recognizes that for purposes of presentment and payment of paper a branch or office of a bank is regarded as a separate and distinct institution.

The term "item" as defined includes nonnegotiable as well as negotiable instruments.

SECTION 2. [Bank of Deposit Is Agent for Collection.]

The purpose of this section is to establish an agency relation of the bank in which paper is deposited and thus protect it, when paper is deposited indorsed unrestrictedly, which is oftentimes the case, from being held liable to its

depositor as owner, as soon as credited to his account. This was so held in City of Douglas v. Federal Reserve Bank, 46 Sup. Ct. 554, notwithstanding there was a custom to charge back in event of dishonor and the contract provided that out-of-town items were expressly credited "subject to final payment." It was pointed out that in the event of dishonor, the bank could ordinarily have recourse upon the depositor as indorser, but in the particular case, the indorser was discharged, because the item had been paid by a worthless draft of the drawee bank, which failed and the bank of deposit was the loser. Banks generally protect themselves by stipulations on deposit slips, signature cards or pass-books against such liability, by declaring that the bank is agent not owner. The above section provides a statutory relation of agency in the absence of agreement to the contrary, but if the bank receives the paper unrestrictedly indorsed, it becomes liable as owner to subsequent parties who act in reliance upon its ownership unless it protects itself as provided in Section 4.

Subsequent collecting banks are defined as sub-agents of the depositor but are authorized to follow instructions of the immediate forwarding bank.

Credits given by agent banks for uncollected paper are revocable and do not make the bank responsible as debtor until the proceeds have been received in money or an unconditional credit therefor has been given which has been requested or accepted (see Secs. 9 and 10). The provision making the bank debtor where an unconditional credit is given which has been requested or accepted applies in all cases where the presentment is by mail, over the counter or through the clearings and is based upon the principle that the bank should be responsible as debtor where it becomes owner of a credit which it is not compelled to accept but which it does accept on its own responsibility upon the books of another bank which fails.

SECTION 3. [Item on Same Bank.]

The majority of courts hold that credit of an item on the same bank is final and cannot be charged back, notwithstanding such item is found not good upon examination of the account. The theory, is that the bank is presumed to know at all times the condition of a customer's account. While it is the bank's duty to the drawer-customer of a check to pay or reject it immediately, the courts have held

that it is competent for the bank to agree with the payee-depositor that payment be deferred for a reasonable time in order to examine the account. In banking practice, deposited checks on the same bank are immediately credited in the depositor's pass-book without opportunity for examination of the drawer's account at the moment and it is clearly unreasonable for the depositor of an item drawn on the same bank to expect an irrevocable credit until the bank has had a reasonable time to inquire into the account. The code fixes a definite rule that such credit shall be provisional subject to revocation which the bank might exercise at any time during the day.

SECTION 4. [Legal Effect of Indorsements.]

The Negotiable Instruments Act defines the legal meaning and effect of certain kinds of indorsements, such as indorsements in blank and special indorsements, which convey title, indorsements "without recourse" which convey title but without liability for non-payment, conditional indorsements which convey title subject to a condition and restrictive indorsements which either constitute the indorsee the agent of the indorser or which vest title in the indorsee as trustee. As to the latter class of indorsements, the courts are in conflict whether certain forms of indorsements are restrictive and agent-creating or unrestricted and title-conveying and Section 4 is designed to clear up this conflict in the case of indorsements "for deposit" and "pay any bank or banker" which have been held both agent-creating and title-conveying in different jurisdictions.

The first paragraph of Section 4 provides the legal effect of an indorsement "for deposit" making same restrictive and providing that the bank is agent and not owner.

The indorsement "pay any bank or banker" is likewise made restrictive and creating an agency relation "unless coupled with words indicating the creating of a trustee relationship." Many collecting banks stamp upon items various forms of which the following is a sample:

> "This Draft is a CASH ITEM and is not to be treated as a deposit The funds obtained thru its collection are to be accounted for to us as a trust and are not to be commingled with other funds of collecting bank."

The words "unless coupled" etc., are inserted to cover such condition.

The section further provides not only in the case of indorsements "pay any bank or banker" but in all cases of restrictive indorsements, whether creating an agency or trust relationship, that such indorsements carry a guaranty of genuineness and authority to make prior indorsements and to save the drawee harmless in case of defective or irregular prior indorsements Most restrictive indorsements are coupled with a guaranty of prior indorsements and drawee banks generally require such guaranty as a prerequisite of payment. It seems proper, therefore, to have this feature incorporated in the law; but it is qualified by the provision "unless such indorsement is coupled with appropriate words disclaiming such liability as guarantor." This would enable any forwarding bank that did not desire to incur a guarantor liability to couple with its indorsement a disclaimer, such as "without guarantor liability" or other form of disclaimer.

The Code provides that where a deposited item is payable to bearer or is indorsed in blank or specially, the bank of deposit remains agent but subsequent holders have the right to rely on the presumption that the bank of deposit is owner; also that like indorsement or delivery of bearer paper by a bank of deposit or a subsequent holder carries like presumption that the indorsee or transferee is owner where there is nothing on the face of the paper or in any prior indorsment to indicate an agency relation of any prior party This provision of the Code is in harmony with existing law, for example (we quote from *Paton's Digest*, Volume 2, pages 1134 and 1135):

> "In Park Bank v. Seaboard Bank, 114 N. Y. 28, a check on the Park Bank for $8. was raised by the payee to $1,800., indorsed *in blank* by him and delivered to the Eldred (Pa.) Bank for collection only. The Eldred Bank endorsed it 'for collection' to the Seaboard Bank in New York, and that bank received payment. It was held that the Seaboard, appearing by the indorsement to be a mere agent, was not liable after it had paid over the money to its principal, the Eldred Bank. Later, in an action by the Park Bank directly against the Eldred Bank, 90 Hun. 285, it was held the

> Eldred Bank was liable, because it was apparently owner of the draft, although, in fact, agent for collection only. The court said: 'In the case of the Seaboard Bank, the agency was disclosed; in the case of the Eldred Bank, it was not. In the presentation of the draft the Eldred Bank represented itself to be the owner of the draft, and the payment was made by plaintiff under those circumstances. It does not seem to need the citation of authorities to show that where money is paid upon a raised draft without any negligence on the part of the person paying the same, it can be recovered from the party to whom it was paid.' ''

It is common for depositors to indorse checks in blank when they are placed on deposit, or specially to the bank, and probably not all banks realize that under such indorsement, although as between bank and depositor, the bank is agent, yet as to all subsequent holders and especially the payor, the bank is liable as apparent owner, in case of raised or altered checks or should the payee's indorsement be a forgery. It has, therefore, been deemed wise to insert a provision that where an item is so deposited or received for collection, the bank may negative the presumption of ownership by writing over the signature of the indorser the words "for deposit" or other restrictive words. This authority would apply to any bank in the collection chain.

SECTION 5. [Duty and Responsibility of Bank Collecting Agents.]

This section is intended to clear up the wide conflict between those decisions holding that the collecting bank is liable for the negligence and defaults of correspondents and those holding the bank not liable, provided it exercises due care. Because of such conflicting decisions and uncertainty in the law of those states where no rule has been declared, the Code provides a definite rule of liability for default of correspondents, namely, the "due care" rule, known as the Massachusetts rule, which is now followed in a majority of the states. In those states following the so-called "New York rule" that a collecting bank is liable for defaults of correspondents and in the other states where the question is unsettled, the banks are compelled to protect themselves by a special agreement. The weight of authority and the better reasoning is in favor of the Massachusetts rule. A

person depositing items is aware that the bank cannot collect it through its personal agents and employees; the ordinary exchange charge, if there is one, is very small, in comparison to the service rendered, and the liabilities assumed by the bank if it be held responsible for the acts and conduct of its correspondent bank beyond the measure of care required in selecting a suitable correspondent, is out of all proportion to such charge.

SECTION 6. [Rules of Ordinary Care in Forwarding and Presentment.]

This section in effect enacts into law the usual banking custom in regard to forwarding and presenting paper.

Custom has sanctioned the practice of forwarding direct to the drawee or payor bank, contrary to the judicial rule that such method of forwarding is negligence, and the enactment of the American Bankers Association recommended measure which authorizes such practice, now in force in the majority of states, has legalized this custom. The Code makes this rule uniform in all states and also legalizes the customary mode of presenting through bank correspondents.

SECTION 7. [Items Received Through the Mail.]

It has always been an uncertain question as to what time in the physical handling of a check received through the mail it is deemed paid. It is to the interest of the drawee or payor bank to fix a definite point of time at which the item shall be deemed paid to avoid trouble and litigation where, for example, an attachment is levied against the customer's account while the check is in possession of the drawee bank or where the drawer seeks to stop payment. The provision only has application to a solvent drawee or payor.

SECTION 8. [Items Lost in Transit.]

While the law is at the present time in accord with the above, a bank will frequently have trouble with its depositor, where the latter has apparently kept no record of the source of an item and it is difficult to get him to assume responsibility and procure a duplicate. When the non-liability of the bank is established in a definite provision of law, it makes it easier to deal with the depositor on this troublesome question. A similar provision is now a part of the statutory law of California.

SECTION 9. [Medium of Payment.]

Methods of payment may be classified as (1) money (2) draft on a bank (3) credit and (4) set-off of exchanged items with settlement of balance by either one of the first three methods.

The principle of Section 9 is to authorize the agent collecting bank to receive, instead of money, without being responsible therefor as debtor, the customary method of settlement for an item by draft on another bank or by exchange of items and settlement of balance by money or draft.

The acceptance of a draft on another bank is the ordinary method of transferring the funds from the custody of the payor bank. If, however, the agent collecting bank, instead of accepting money or such draft on another bank, chooses to allow the money to remain with the payor bank and the latter to remain debtor, by accepting a credit on its books, or an unconditional credit on the books of any other bank, this method of settlement of the agent bank's own choosing, under which the payor or some other bank is allowed to remain debtor, instead of the fund being transmitted to the owner, makes the agent collecting bank itself responsible as debtor therefor.

SECTION 10. [Medium of Remittance.]

This applies the principle underlying Section 9 to the case of the remitting bank, after the proceeds are collected.

SECTION 11. [Election to Treat as Dishonored Items Presented by Mail.]

The purpose of this Section is to permit the agent collecting bank, at its option, to continue the liability of the drawer or maker and indorsers upon a check, not presented over the counter or through the clearing house, but by mail, where the drawee or payor defaults in making payment because of its insolvency.

Presentment direct to the drawee by mail (as distinguished from mailing to an independent agent at the place of the drawee) is customary and legally sanctioned by statute in a number of states and by this Code and it is the opinion of a number of banking experts (although all are not agreed) that the drawer who gives his check upon a bank which cannot pay, should not be relieved of his obligation by the mere charging of the check to his account and the issuance by the drawee of a worthless draft therefor

but should stand for the solvency of his bank, which is his paying agent, until the latter's draft is at last paid.

Accordingly four contingencies are provided in which the item may be dishonored and the liability of the drawer continued at the option of the agent collecting bank. Where such liability is continued, the recourse is upon the drawer and prior parties and not upon the failed bank. In any case where it is found impracticable, by reason of inability to identify prior parties to an item forwarded to the drawee for which it has attempted to settle in any of the ways above mentioned, the option need not be exercised and in such event the draft or credit given by the drawee or payor will operate as payment of the original item and the owner will have recourse as preferred creditor under Section 13.

Should it be found undesirable in any state to adopt the policy declared in this section the same can be omitted; and in such event Section 12 should also be omitted and also the opening words in paragraph 2 of Section 13, "Except in cases where an item or items is treated as unpaid and dishonored as provided in Section 11."

SECTION 12. [Notice of Dishonor of Items Presented by Mail.]

The purpose of this section is to supplement the Negotiable Instruments Act which provides for notice of dishonor to preserve the liability of prior parties when an instrument is dishonored by non-acceptance or non-payment. It is intended to cover the new forms of dishonor provided in Section 11. The general requirements of the Negotiable Instruments Act as to giving notice of dishonor will still apply.

SECTION 13. [Insolvency and Preferences.]

There is much conflict in the decisions over the right to preference in payment of collection proceeds out of the assets of a failed bank. The purpose of this section is to establish uniform rules based on the better reasoned decisions. Except where the failed bank (whether drawee or payor or other collecting bank) has been accepted as debtor for such proceeds by reason of a requested or accepted credit given by it on its own books or on the books of any other bank, a trustee relation is created with respect to such proceeds both in the case of the drawee or payor after the mony has been taken out of the account of the drawer or maker and in the case of an agent collecting bank other

than the drawee or payor, which has received the proceeds in any form; and the owner of the item is entitled to preferential payment out of the assets of the failed trustee whether the proceeds can be traced and identified into a specific fund or not.

In case an item is received by a bank which fails before the actual payment or collection thereof, provision is made for return of the item where in its possession or that of the receiver. Furthermore, the provisions of Section 13 do not apply to items presented by mail which, at the election of the presenter, are treated as dishonored by non-payment according to the provisions of Section 11.

Sections 14 to 19 inclusive are self explanatory.

UNITED STATES CIRCUIT COURT OF APPEALS FOURTH CIRCUIT.

No. 3735.

W. H. Spradlin, Receiver of the Elkin National Bank,
Appellant,

versus

Royal Manufacturing Company, a corporation,
Appellee.

Appeal from the District Court of the United States
for the Middle District of North Carolina,
at Winston-Salem.

(Argued October 26, 1934. Decided November 19, 1934.)

Before Parker, Northcott and Soper, Circuit Judges.

John J. Ingle and John H. Folger for Appellant, and
E. C. Bivens for Appellee.

Parker, Circuit Judge:

This is an appeal from a decree holding a claim of the Royal Manufacturing Company for $3,483.73 to be a lien on the assets of the failed Elkin National Bank in hands of its receiver. The claim arose out of a draft on the Chatham

Manufacturing Company which was sent to the bank for collection. The company last named paid the draft by a check drawn against its deposit account with the bank, and the bank remitted for the collection by draft on one of its correspondents, but failed before this draft could be paid. There was, of course, no augmentation of the assets of the bank as a result of the collection, but merely a shifting of credits, and consequently no basis for the declaration of a trust. *Lifsey v. Goodyear Tire & Rubber Co.* (C. C. A. 4th) 67 Fed. (2d) 82, 83; *Ellerbe v. Studebaker Corporation of America* (C. C. A. 4th) 21 Fed. (2d) 993, 995; *Larabee Flour Mills v. First Nat. Bank* (C. C. A. 8th) 13 Fed. (2d) 330, 331. The learned judge below was of opinion, however, that the assets of the bank were subjected to a lien to the amount of the collection by reason of the proviso appearing in Section 218 (e) (14) of the North Carolina Code of 1927.

Section 218 (e) of the North Carolina Code is composed of twenty-three subsections all of which relate to the liquidation of state banks. Subsection 14 thereof, which contains the proviso in question, is as follows:

"(14) Declaration of Dividends; Order of Preference in Distribution.—At any time after the expiration of the date fixed by the Chief State Bank Examiner, or the duly appointed agent, for the presentation of claims against the bank, and from time to time thereafter, the Corporation Commission, out of the funds in its hands, after the payment of expenses and priorities, may declare and pay dividends to the depositors and other creditors of such bank in the order now or hereafter provided by law; and a dividend shall be declared when and as often as the funds on hand subject to the payment of dividends shall be sufficient to pay ten (10) per centum of all claims entitled to share in such dividends. In paying dividends and calculating the same, all disputed claims and deposits shall be taken into account but no dividend shall be paid upon such disputed claims and deposits until the same shall have been finally determined. The following shall be the order and preference in the distribution of the assets of any bank liquidated hereunder: (1) Taxes and fees due the Corporation Commission for examination or other services; (2) wages and salaries due officers and employees of the bank, for a period of not more than four months; (3) expenses of liquidation;

(4) certified checks and cashier's checks in the hands of a third party as a holder for value and amounts due on collections made and unremitted for or for which final actual payment has not been made by the bank; (5) amounts due creditors other than stockholders. The word 'asset' used herein shall not be deemed to include bailments or other property to which such bank has no title. Provided, that when any bank, or any officer, clerk, or agent thereof, receives by mail, express or otherwise, a check, bill of exchange, order to remit, note, or draft for collection, with request that remittance be made therefor, the charging of such item to the account of the drawer, acceptor, indorser, or maker thereof, or collecting any such item from any bank or other party, and failing to remit therefor, or the nonpayment of a check sent in payment therefor, shall create a lien in favor of the owner of such item on the assets of such bank making the collection, and shall attach from the date of the charge, entry or collection of any such funds. A statement of all dividends paid shall be filed in the office of the clerk of the Superior Court in the pending action, and said statements shall show the expenses deducted and the disputed claims and deposits considered in determining said dividend."

It is clear, we think, that even if this proviso be construed as having relation to solvent banks as distinguished from those in liquidation, it cannot affect national banks. It has been held that these banks have no power to pledge their assets to secure a private deposit (*Texas Pac. Ry. Co. v. Pottorff*, 291 U. S. 245, 253); and one of the reasons for this holding is that to permit such pledge would be inconsistent with many provisions of the national bank act which are designed to insure a ratable distribution of assets among creditors. The same reasoning would forbid the creation of a lien on assets as security for funds collected. And, of course, if the creation of such a lien be beyond the powers of the bank, it could not be created by act of the state legislature; for the legislature could not provide that action on the part of the bank should give rise to a lien which the bank, by reason of the limitations imposed upon it by act of Congress, was powerless to create.

But it is clear that the statute in question was not intended to have application to solvent banks. Quite apart from the fact that it is a proviso to one of the sub-sections of a statute dealing with the liquidation of insolvent banks,

it appears that it can have no practical application except in connection with their liquidation. The lien created, although it is to attach from the date of the charge, entry or collection, arises only upon "failing to remit" or "the non-payment of a check sent in payment"; and it is manifest that a solvent bank will not fail to remit collections or permit a check sent in payment of a collection to remain unpaid. It is only in case of banks which have failed, therefore, that the statute can have any practical application; and the lien which it creates is of such a character that it can be enforced only by a liquidation of the bank. See *Lewis v. Fidelity & Deposit Co.*, 292 U. S. 559 at 563 and 567. The statute must be construed, therefore, as relating to the distribution of assets in the hands of banks which have failed; for "in whatever language a statute may be framed, its purpose must be determined by its natural and reasonable effect." *Collins v. New Hampshire*, 171 U. S. 30, 34; *Morgan v. Louisiana*, 118 U. S. 455, 462; *Henderson et al. v. Mayor of New York*, 92 U. S. 259, 268. So construed, it can have no application to the assets of national banks; for the national banking act provides how the assets of insolvent national banks shall be distributed. 12 U. S. C. A. 194. And it is well settled that state statutes cannot affect this distribution. *Davis v. Elmira Savings Bank*, 161 U. S. 275; *Easton v. State of Iowa*, 188 U. S. 220; *Old Company's Lehigh v. Meeker* (C. C. A. 2d), 71 Fed. (2d) 280; *Fiman v. South Dakota* (C. C. A. 8th), 29 Fed. (2d) 776, 777; *First Nat. Bank of Chicago v. Selden* (C. C. A. 7th), 120 Fed. 212.

The case of *Lewis v. Fidelity & Deposit Co.*, 292 U. S. 559, relied upon by appellee, is in reality an authority against its position. In that case a statute of Georgia, creating a general lien on the assets of banks as security for deposits of state funds, was held to have application to a national bank merely because the act of Congress of June 25, 1930, c. 604, 46 Stat. 809, 12 U. S. C. A. 90, authorized a national bank to give security for a deposit of public funds of the same kind as authorized by state law for state banking institutions. The Supreme Court said that no lien under the Georgia statute arose in 1928 when the deposit was made, and that the judgment of the court below sustaining the lien would have been reversed but for the enactment by Congress of the Act of 1930. See p. 564. Here

there is no act of Congress authorizing the creation of a lien on the assets of a national bank as security for collections; and the act of the North Carolina legislature can no more create a lien on the assets of a national bank than could the Georgia statute without the aid of the act of 1930.

We do not interpret the proviso as having been intended to make the collecting bank the agent of the holder of the item sent for collection, which was the purpose of the sections of the uniform bank collection code under consideration in *National Bank of America v. U. S. F. & G. Co.* (C. C. A. 7th), 71 Fed. (2d) 618, 619, and *Old Company's Lehigh v. Meeker, supra.* Nevertheless, under the rule recognized in this Circuit, the bank here was the agent of the owner of the draft for the purpose of making the collection and remitting the proceeds. *Ellerbe v. Studebaker Corporation* (C. C. A. 4th), 21 Fed. (2d), 993, 994; *Lifsey v. Goodyear Tire & Rubber Co.* (C. C. A. 4th), 67 Fed. (2d) 82, 83. But under the authority of these cases, appellee is not entitled to have a trust declared or to receive preferential payment from the assets in the hands of the receiver, since it has failed to show that these assets have been augmented as a result of the collections.

For the reasons stated, the decree appealed from will be reversed.

Reversed.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934.

No. 338

DAVID H. JENNINGS, Receiver of the National Bank of America, and NATIONAL BANK OF AMERICA,
Petitioners,
v.
UNITED STATES FIDELITY AND GUARANTY COMPANY,
Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI.

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RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI.

I.

OPINION.

The opinion of the Circuit Court of Appeals for the Seventh Circuit is reported in 71 Fed. (2d) 618, and also appears at Record pages 46-54. That of the District Court appears in 4 Fed. Supp. 569, and at Record pages 27-30.

II.

JURISDICTION.

It appears that jurisdiction exists in the Supreme Court to entertain the petition for certiorari. The suit pertains to the winding up of the affairs of an insolvent national bank (*Larabee Flour Mills v. First Nat. Bank* (8 C. C. A.), 13 Fed. (2d) 330), and was within the jurisdiction of the District Court to decide. Judicial Code, Sec. 24, par. 16; 28 U. S. C. A. 41 (16). The Circuit Court of Appeals had jurisdiction of the appeal. Judicial Code, Sec. 128 (a); 28 U S. C. A. Sec. 225 (a). The petition for certiorari was filed (August 31) within three months after final judgment (June 4, 1934), and the Supreme Court has jurisdiction to entertain the petition. Sec. 240 (a) Judicial Code; 28 U. S. C. A. Sec. 347.

III.

STATEMENT OF CASE.

The suit was brought by Respondent against the petitioning receiver of National Bank of A..erica, doing business at Gary, Indiana, and the bank, and it is in substance a suit in equity for the separation and payment from the cash in the receiver's possession of an amount equal to the amount of the proceeds of a check owned by Respondent and collected and held in trust by the bank as agent for Respondent.

It is not a suit seeking preferential payment of a debt out of assets of the bank, but instead it is one to recover that which is not an asset of the bank but which belongs to Respondent as the bank's principal. The relationship of debtor and creditor did not exist between them.

Neither is the suit predicated on the preference provisions contained in Sec. 13 of the Indiana Bank Collection Code to which the petition and supporting brief make reference. Only that part of the state statute is relied on which applied to the bank while acting as a collecting bank in this transaction and which fixed the relations of the parties toward each other and toward the item and the proceeds collected thereon. On the basis of those relations thus fixed, the right to recover is further predicated on well-established principles of equity recognized and enforced in such cases by Federal Courts.

The proceeds of Respondent's check were collected, received and held by National Bank of America, and are now held by its receiver, under the circumstances (R. 16-26) following:

Respondent, United States Fidelity and Guaranty Company, became the owner on December 30, 1931, at Indianapolis, Indiana, of a check for $2,196.89 drawn on a Gary, Indiana, bank, and on that day deposited it in its Indianapolis bank for collection. The next day National Bank of America, at Gary, received the check from Fletcher American National Bank of Indianapolis for collection and remittance.

The Uniform Bank Collection Code was then in force in Indiana. Sec. 3861.1 et seq. Burns' Ann. Ind. Stat., Supp. of 1929. By its terms (Sec. 3861.1) this statute applied to all banks in the State. Under its provisions (unless otherwise agreed, which was not done) National Bank of America as the last bank receiving the item for collection became subagent of the depositor (Respondent), and the statute gave it authority as such agent collecting bank (Sec. 3861.9),

without becoming a debtor to Respondent, to receive in lieu of money for the check payment in such form as was customary in the local clearing house, including checks upon itself which the drawee bank might present in the clearings.

National Bank of America collected Respondent's check on December 31st, 1931, through the Gary Clearing House, and in payment therefor received checks drawn on itself, which the bank upon which Respondent's item was drawn presented at the clearings. This check was then charged to the drawer's account and delivered up as a cancelled check.

After the collection was so made by National Bank of America, it, on the same day, drew its draft on a Chicago correspondent and mailed it to the forwarding bank at Indianapolis, which in turn mailed the draft to the Chicago bank for payment. National Bank of America having failed to open on the morning of January 4, 1932, and the draft arriving at Chicago later that day, payment of the draft was refused. The draft has been returned to the receiver.

The cash and cash items in possession of National Bank of America, and later in possession of the receiver, have at all times exceeded, and now exceed, the amount of the proceeds from Respondent's check. Respondent has received nothing on the check and has sustained a charge-back of the credit received at the time of deposit for collection.

The facts were specially found by the District Court, and the conclusions of law and decree were in Respondent's favor. The Circuit Court of Appeals affirmed, except as to interest on the amount.

IV.

SUMMARY OF ARGUMENT.

PROPOSITION I.

No valid reason for allowance of the writ is shown.

Point 1.

The decision, decree, and opinion of the Circuit Court of Appeals are not in conflict with any decisions, or principles established in decisions, of the Supreme Court, but are in harmony therewith.

(a) In no case has the Supreme Court held that a transaction by a national bank, such as the collection by it of an item for another is immune from effect of such state laws as the Indiana Bank Collection Code. On the contrary, the Supreme Court did on the very day of the decision by the Circuit Court of Appeals (June 4, 1934) reaffirm and apply the principle that transactions by national banks are subject to State laws which do not interfere with the functions of such banks as agencies of government and which do not conflict with Federal law. *Lewis v. Fidelity and Deposit Company*, 54 Sup. Ct. Rep. 848, 851. The principle that national banks are controlled by state laws in most of their transactions has long been established by the decisions of this Court. *McClellan v. Finch*, 164 U. S. 347, 356, 357.

State statutes governing collections by banks do apply to national banks so as to fix their relations to the items and to their owners. *Federal Reserve Bank v. Malloy*, 264 U. S. 160, 164.

(b) Nor is the decision in conflict with any decision of the Supreme Court in that it awards to the owner the proceeds of a collected item held in trust for him by the bank. In *Capital National Bank of Lincoln v. First National Bank, and MacFarland, Receiver*, 172 U. S. 425, 433, this Court said it knows of no provision of the banking act which assumes to appropriate trust funds in the possession of insolvent banks. To the same effect is *Scott v. Armstrong*, 46 U. S. 499, 510.

Point 2.

Neither is the decision in conflict with decisions of other circuits when proper distinctions are observed. It is true that there are decisions in other circuits which hold that the basis for a trust fails when an item received for collection is misused to pay the bank's own debts to, or through, a clearing house and the clearing house balance is against the bank. But those decisions were made without reference to the effect of the Uniform Bank Collection Code, which now authorizes the agent bank to collect through a clearing house and to receive in payment, in lieu of money, any customary settlement at a local clearing house, and which gives an entirely different legal effect to such a transaction than the Courts gave it in the absence of such authority.

Point 3.

The decision and opinion of the Circuit Court of Appeals observe the rule as to augmentation and tracing, and finds the rule satisfied under the facts in the light of the effect of the provisions of the Uniform Bank Collection Code which entered into the transaction. The decision in this respect is not against weight

of authority but is in harmony with the authorities requiring a showing of augmentation and tracing. Other Courts not having had occasion to consider the effect of the Uniform Bank Collection Code as affecting the question of whether augmentation and tracing exist under such facts as shown in the record, it cannot fairly be said that the decision is against any authority, much less against the weight of authority.

PROPOSITION II.

The case was correctly decided, and the opinion of the Circuit Court of Appeals is lucid and complete on all points involved.

Point 1.

Contracts of National banks are generally governed and construed by state laws, and their property rights are also based on state law.

McClellan v. Chipman, 164 U. S. 347, 356, 357;
Lewis v. Fidelity and Deposit Company (1934), 54 Sup. Ct. Rep. 848, 851.

State statutes governing collections of items by banks enter into such transactions and determine the relations, authority and rights of national, as well as state banks.

Federal Reserve Bank v. Malloy, 264 U. S. 160, 162, 164.

Point 2.

It not having been otherwise provided by agreement, and Respondent's check having been deposited

for collection only, National Bank of America was Respondent's sub-agent for the collection of the check and for remittance of the proceeds in virtue of provisions of state law.

Sections 1-2, Uniform Bank Collection Code, ch. 164, Indiana Acts of 1929;
Sections 3861.1-3861.2, Vol. IV, Burns' Ann. Ind. Stat. 1929 Supp.

Point 3.

By the contract made, into which the provisions of said state law entered and formed a part, National Bank of America as "agent collecting bank" was authorized to receive "*in payment*" of Respondent's check "without becoming responsible as debtor therefor," in lieu of money, the exchanged checks drawn on it and presented to it through the clearing house by Gary State Bank.

Sec. 9, Ch. 164, Indiana Acts 1929;
Sec. 3861.9, Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp.

In the absence of statutory authority to receive payment in that manner and form, National Bank of America would have had authority to receive in payment only legal tender money.

Federal Reserve Bank v. Malloy, 264 U. S. 160, 165.

Point 4.

Payment for Respondent's item having been received by National Bank of America in said manner and form, it did not become responsible as debtor there-

for and it remained Respondent's sub-agent in respect thereto. Under the agreed facts, the proviso in Sec. 9 did not apply.

Sec. 9, Ch. 164, Indiana Acts of 1929;
Sec. 3861.9, Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp.

Point 5.

The fiducial relation of National Bank of America to the proceeds of Respondent's check was not changed by the abortive effort to remit by draft on Chicago, in that the draft did not constitute an unconditional credit requested or accepted by Fletcher American National.

Sec. 10, Ch. 164, Indiana Acts of 1929;
Sec. 3861.10, Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp.,

and in that the unpaid draft (later returned to the receiver) did not constitute payment by National Bank of America.

Jefferson Standard Life Ins. Co. v. Wisdom, (5th C. C. A.) 58 Fed. (2nd) 565, 566.

Point 6.

The proceeds of Respondent's check (in the form of checks drawn on the collecting bank) were the same as cash to the collecting bank, and when it retained an amount in cash and cash items equal to the amount of said proceeds which it otherwise would have paid out (R. 23) there was in legal effect a substitution of that amount of cash and cash items for the amount of said proceeds in their first form, and the collecting

bank remained a fiduciary toward said proceeds in their substituted form (Sec. 9 of said Code). In that situation true augmentation of the cash and cash items held by the collecting bank is shown, for they were greater by the amount thus collected as a direct result of the collection.

Ellerbe v. Studebaker Corp. of Am. (4th C. C. A.) 21 Fed. (2d) 993, 996, 997;
Schumacher v. Harriett (4th C. C. A.) 52 Fed. (2d) 817, 819, 820

Point 7.

It appearing that $2,196.89 in amount of the collecting bank's cash and cash items were in legal effect substituted for the checks lawfully received from Gary State Bank in payment for Respondent's check, the collecting bank remained a fiduciary in respect to that amount and equity will, under modern rule, in a proper proceeding segregate said proceeds *in amount* from the aggregate of said cash and cash items if the aggregate in the receiver's hands includes said amount.

Ellerbe v. Studebaker Corp. of Am. (4th C. C. A.), 21 Fed. (2d) 993, 996, 997.

Point 8.

Said cash and cash items having at all times remained in excess of the amount of said proceeds held in trust, the trust fund is clearly traced into the receiver's hands, under the presumption that whatever may have been paid out was paid out of the bank's own.

Peoples Nat. Bank v. Moore (8th C. C. A.), 25 Fed. (2d) 599, 601;

Schumacher v. Harriett (4th C. C. A.), 52 Fed. (2d) 817, 818.

Point 9.

The receiver took said cash and cash items subject to the trust therein in Respondent's favor to the amount of said proceeds from said check, and to the extent of the amount of said proceeds said cash and cash items do not constitute assets of the bank for ratable distribution, but that amount thereof belongs to Respondent and the decree properly separates that amount and orders it paid to Respondent.

Capital Natl. Bank v. First Natl. Bank of Cadiz, 172 U. S. 425, 433;

Ellerbe v. Studebaker Corp. of Am. (4th C. C. A.), 21 Fed. (2d) 993, 997;

Peoples Natl. Bank v. Moore (8th C. C. A.), 25 Fed. (2d) 599, 601;

Jefferson Standard Life Ins. Co. v. Wisdom (5th C. C. A.), 58 Fed. (2d) 565, 566;

Scott v. Armstrong, 146 U. S. 499, 510.

ARGUMENT.

THERE IS NO CONFLICT IN DECISIONS.

There is no conflict between the decision of the Circuit Court of Appeals in this case and decisions of either the Supreme Court or of other Circuit Courts of Appeal. Instead, they are in harmony.

The decision in no wise conflicts with Federal law governing distribution of assets of failed national banks, nor does it give effect to any state law which conflicts with Federal law. The decision is not predicated on any preference provisions contained in Sec. 13 of the Indiana Bank Collection Code. The decision does recognize the effect of those provisions in said Code which govern the collection transaction in question and which operated to fix the agency and trust relationships of the bank toward the owner and toward the item and the proceeds therefrom. And in view of those relationships, the decision favors recovery by Respondent after the court first found that the cash and cash items in the bank's possession were augmented by the proceeds and that, the amount of such cash and cash items not having at any time fallen below the amount of such proceeds, those proceeds are now among the cash and cash items held by the receiver under the presumption that the amount held in trust by the bank was kept sacred and is being held by the receiver subject to the trust. Thus, what the decision awards to Respondent is not an asset of the bank, but it belongs to Respondent.

The provisions in the Indiana Bank Collection Code which, under the facts, defined the bank as Respond-

ent's subagent (Sec. 3861.2, Burns' Ann. Ind. Stat., 1929 Supp.), and which (Sec. 3861.9, id.) authorized it as such agent to collect the item for Respondent and, *without becoming responsible as debtor*, to receive, in lieu of money, payment in such form as was customary at the local clearing house, including checks upon itself, clearly were not in derogation of the bank's functions as an agency of government. This was a purely private commercial transaction. Neither do those statutory provisions conflict with any Federal law, for none has been enacted to govern such transactions.

Hence, the provisions of the Indiana statute just referred to did govern the collection transaction and did operate to fix the relationships of the parties thereto toward each other and toward the subject matter of the transaction under authority of *McClellan v. Chipman*, 164 U. S. 347, 356, 357; *Lewis v. Fidelity and Deposit Company* (1934), 54 Sup. Ct. Rep. 848, 851; *Federal Reserve Bank v. Malloy*, 264 U. S. 160, 164. Thus, the point in the decision by the Circuit Court of Appeals that those statutory provisions were applicable is in harmony, rather than in conflict, with the decisions of the Supreme Court.

The point to the decision that trust funds coming in possession of the receiver of a national bank belong to the owner and may not be appropriated to make assets is also recognized in the decisions of the Supreme Court. *Capital Nat. Bank v. First Nat. Bank of Cadiz*, 172 U. S. 425, 433; *Scott v. Armstrong*, 146 U. S. 491, 510.

Nor is there conflict in this decision and those of other circuits when proper distinctions are observed. None of the decisions from other circuits to which Peti-

tioners make reference involved the effect upon such transactions of the applicable provisions contained in the Uniform Bank Collection Code. Some of the cited cases do hold that where a bank receives an item for collection and then misuses it to pay its own obligations at a clearing house and the clearing house balance is against it, the basis for a trust fails. But the Code, where in force, now authorizes agent banks to collect items through clearing houses, and to receive payment in things other than money without the relationship of debtor and creditor arising. The legal effect of such an authorized transaction under the Code is obviously far different than where a bank violates its agency relationship and misuses the item entrusted to it by paying its own debts with the item. When a collection is made, and payment received, in a mode authorized by the Code, as here, there is a valid distinction which prevents conflict between this decision and those made with a view to the general law as it obtains where no such Code is in force. It can, therefore, not fairly be said that this decision conflicts with those from other circuits, or that it is against weight of authority. There seem to be no other decisions in which these code provisions were considered.

The Case Was Correctly Decided.

The Indiana bank collection code does have the effect given it by the decision of the Circuit Court of Appeals. By its terms (Sec. 3861.1, Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp.) it defines "bank" as meaning "any person, firm or corporation engaged in the business of receiving and paying deposits of money within this State." In Section 2, the Act provides that,

unless otherwise agreed, a bank receiving an item on deposit for collection, and all subsequent banks receiving it for that purpose, are agents and subagents, respectively, of *the depositor* (Sec. 3861.2, Vol. IV, Burns' Ann. Ind. Stat. 1929 Supp.). And in Section 3 (same citation), the Act preserves the agency relation notwithstanding certain forms of indorsements.

In virtue of the agreed facts and in virtue of said Sections 1, 2 and 3 of said Act, National Bank of America became the sub-agent of Respondent for the purpose of collecting Respondent's check and for the purpose of remitting therefor. It was an "agent collecting bank" within the meaning of Sec. 9 of said Act (Sec. 3861.9, Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp.).

It is said Section 9, which changed the law from what it was in respect to the authority of such agent collecting banks to receive payment for items in collection in forms other than money without becoming debtor therefor, that Respondent contends has a vital bearing on the question of whether there was true augmentation of the cash and cash items held by National Bank of America after the clearing house transaction of December 31st.

As a matter of general law an agent collecting bank had no authority to receive in payment of the item in collection anything other than legal tender money. *Federal Reserve Bank v. Malloy*, 264 U. S. 160, 165. Much less did an agent bank have authority to use an item entrusted to it for collection for the purpose of paying its own obligations at a clearing house or otherwise. The clearing house cases referred to under Petitioners' Proposition III (pp. 19-22) are

cases where the collecting banks misused the items entrusted to them, and the construction placed on such transactions was that the items were wrongfully used for the payment of their own debts to others.

Sec. 9 of the Uniform Bank Collection Code now legalizes the practice of clearing items held in trust for collection through clearing houses, but the Act places an entirely *different construction* on such transactions than the Courts had given them in the absence of such authority, and gives them an entirely different legal effect.

Whereas, the construction and effect was that an item in collection so used, was wrongfully used as a means of payment of the collecting bank's own debt, and whereas the collecting bank had no authority to receive payment in any form other than money, Section 9 of the Code now authorizes the agent collecting bank to "receive *in payment* of an item without becoming responsible as debtor therefor, whether presented by mail, through the clearing house or over the counter of the drawee or payor, in lieu of money, either (a) * * * or (b) * * * or (c) *such method of settlement as may be customary in a local clearing house or between clearing banks or otherwise.*" Sec. 3861.9, Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp. By proviso to (c) in Sec. 9, it is provided that if the agent collecting bank shall request or accept an unconditional credit which has been given to it on the books of the drawee or payor or on the books of any other bank then the agent bank shall become debtor for the item and responsible therefor as if the "*proceeds*" were actually received by it in money. This did not happen in this case.

Thus, when National Bank of America exchanged Respondent's check on Gary State Bank for checks which the latter held against the former at the clearing house transaction of December 31st, Respondent's check was not, in the eye of of said Sec. 9, used to pay a debt of National Bank of America, but the check was collected by a method expressly authorized in said Sec. 9, and by which the collecting bank *received in payment* the checks upon it which it received in exchange. That which the collecting bank received from Gary State Bank is referred to in the proviso to clause (c) of Sec. 9 as "proceeds." Moreover, since National Bank of America did not request or accept an unconditional credit or for the item on the books of Gary State Bank or on the books of any other bank, it did not become responsible as debtor for either the check or for the "proceeds" of the check.

The "proceeds" thus "received in payment" were the same as cash to the collecting bank, and they were in contemplation of Sec. 9 automatically reflected in the cash and cash items held by the collecting bank after said clearing house transaction, because said cash and cash items became instantly relieved from the obligations of the checks received in exchange to the extent of the amount of Respondent's check. What occurred in legal effect was a substitution of cash and cash items held by National Bank of America to the extent of $2,196.89, in amount, for checks upon it which it received *as agent* in payment of Respondent's check. It is expressly stipulated in the facts (R. 23) that but for said collection of Respondent's check through the local clearing house, National Bank of America would that day *actually have paid* to the clearing house exactly $2,196.89 *more* than it did pay.

Moreover, the obvious reason why the bank did not pay out that additional sum on December 31st was due solely to the fact that Sec. 9 of the code authorized it as Respondent's agent to "receive payment" of the check by such a method as would have that precise effect and to the fact that pursuant to said authority payment of the check was received by such a method.

As to the amount of said proceeds thus involved in the total of the cash and cash items held by the bank after said clearing house settlement of December 31st, National Bank of America was a fiduciary. The bank did not become debtor for said proceeds, but continued to be agent in respect thereof under the facts because of the express provisions of Sec. 9 of said Act.

Hence, there was true augmentation of said cash and cash items by the amount of said proceeds toward which the bank remained a fiduciary. In view of the provisions of said Sec. 9, it was not necessary to support a trust as to said proceeds that there be augmentation in the technical sense of new legal tender money brought into the bank from outside. The checks received in exchange were, however, in a practical sense new money. This is not a case where a bank wrongfully used an item, entrusted to it for collection, to pay its own debt and where the result merely was a decrease in its own debts. It is a case where, pursuant to authority of Sec. 9 of said Code, the bank received "in payment" for Respondent's check other checks upon it and which it in legal contemplation held as proceeds in trust. A necessary result of receiving payment in that form under authority of said Sec. 9 is that a substitution of cash and cash items for the checks received in exchange occurred in legal effect to the extent of

the amount of said proceeds, and the facts are (R. 23) that the collecting bank paid out exactly that much less than it would otherwise have paid. Thereafter, the cash and cash items held by the bank included an amount which was equal to the amount of said proceeds, and as to the amount which represented said proceeds the bank was a fiduciary in respect thereof in virtue of the provisions of said bank collection code. Said cash and cash items were, therefore, greater by the amount of said proceeds as a result of said collection. When that is the result there is true augmentation. *Ellerbe v. Studebaker Corp. of America* (4th C. C. A.), 21 Fed. (2d) 993, 997. In that case the Court used this language:

> "* * * there can be no doubt that as a result of the collection of the draft of complainant, the assets which came into the hands of the receiver were greater by the amount of the collection than they would have been had the collection not been made, and consequently that there was exactly that much more for division among creditors than there would have been otherwise."

The operation and effect of Sec. 9 of the Code in this transaction at once distinguishes this from the cases cited at pages 19-22 of Petitioners' brief to the effect that if the clearing house balance is against the bank which wrongfully uses a check held for collection to pay its own debts there is not augmentation shown. Those cases, and the reasons for the way they are decided, do not control here where the check was not used to pay a debt but where under authority of Sec. 9 of the Code the agent bank "received payment" for the check by receiving in exchange checks drawn upon it.

Where a collection is thus made under express authority of said Code, the accident of which way a clearing house balance may be is immaterial, for in either case the bank, as agent, "receives payment" for the item and comes in possession of "proceeds," within the meaning of said Sec. 9.

Having shown, we think, that the cash and cash items of the collecting bank were truly augmented by the amount of the proceeds from Respondent's check, it remains to be shown that those proceeds are traceable into the cash and cash items now in the receiver's hands. If they are shown to be there, then to the extent of $2,196.89, in amount, the cash and cash items now in the receiver's hands do not constitute assets of the bank and that much does not go to creditors but belongs to Respondent and goes to it. It is only that which belongs to the bank that is required to be distributed ratably to creditors. *Scott v. Armstrong*, 146 U. S. 499, 510; *Capital Nat. Bank of Lincoln v. First Nat. Bank of Cadiz*, 172 U. S. 425, 433; *Jefferson Standard Life Ins. Co. v. Wisdom* (C. C. A.), 58 Fed. (2d) 565, 566.

The abortive effort at remittance by draft did not change the relation of National Bank of America toward said proceeds. On the facts of the case Fletcher American National, as agent, had a right to receive the draft, but did not become debtor therefor (Sec. 3861.10, Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp.). The draft was not paid by Continental and was later returned to appellant receiver. Under such circumstances National Bank of America continued as a fiduciary in respect to said proceeds. *Jefferson Standard Life Ins. Co. v. Wisdom* (C. C. A.), 58 Fed. (2d) 565, 566.

The agreed facts are (R. 26) that the cash and cash items held by the bank after said collection was made never fell below the amount of said proceeds held in trust and that they now exceed that amount. Under modern rule, that sufficiently traces said proceeds into funds in the hands of the receiver so as to entitle Respondent to have a trust declared therefor and to have the amount separated and paid to it. *Ellerbe v. Studebaker, etc.* (4th C. C. A.), 21 Fed. (2d) 993, 996; *Schumacher v. Harriett* (4th C. C. A.), 52 Fed. (2d) 817, 818; *Jefferson Standard Life Ins. Co. v. Wisdom* (5th C. C. A.), 58 Fed. (2d) 565, 566; *Peoples Nat. Bank v. Moore* (8th C. C. A.), 25 Fed. (2d) 599, 601.

Petitioners' contention that segregation of the proceeds of the check by the bank must be shown is erroneous. If those proceeds are traced into the mass of cash items held by the receiver, equity will, under modern rule, order their separation *in amount. Schumacher v. Harriett* (4th C. C. A.), 52 Fed. (2d) 817, 818; *Ellerbe v. Studebaker, etc.* (4th C. C. A.), 21 Fed. (2d) 993, 996.

The case of *Allied Mills, Inc. v. Horton*, 65 Fed. (2d) 708, recently decided by the Circuit Court of Appeals for the Seventh Circuit in which it was held that augmentation did not appear where the collecting bank was also the paying bank, is distinguishable from the instant case. Here, we have another than the collecting bank as payor of the item, and we also have the provisions of the Bank Collection Code entering into the transaction with the effect already shown. It does not appear in the cited case that the collecting bank became fiduciary toward any proceeds received "in payment" of the item. That case obviously does not control this case.

The cases cited by Petitioners' brief do not support their contention that it was error to enjoin the receiver from otherwise using so much of the cash and cash items in his hands as is required to satisfy the decree. The facts and the law show that the amount awarded by the decree belongs to appellee and not to the bank or its receiver. The facts also show (R. 26) that the receiver intends to treat the proceeds of Respondent's check, as embodied in the cash and cash items in his hands, as assets for ratable distribution. That would be a wrongful use of what belongs to Respondent, and it obviously was proper to enjoin the receiver from misusing that which he holds for Respondent. The order does not preclude distribution of any assets belonging to the bank.

The equities are clearly with Respondent. The bank collected Respondent's check as agent and continued as such in respect to the proceeds. The collection was made on about the last day the bank was open for business. Those proceeds belonged not to the bank, but to Respondent. The bank's creditors have no just claim to what the bank thus held as agent for Respondent. The decree only awards to Respondent what it was intended to get from its agent.

It is respectfully submitted that the writ of certiorari should not be allowed.

Respectfully submitted,

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ARTHUR L. GILLIOM,
OWEN PICKENS,
Attorneys for Respondent.

APPENDIX.

Pertinent Parts of Uniform Bank Collection Code, Ch. 164 Indiana Acts of 1929.

"Banks—Collection and Payment of Checks, Other Instruments—Definitions.

Section 1. Be it enacted by the general assembly of the State of Indiana, That for the purposes of this code:

(a) The term "bank" shall include any person, firm or corporation engaged in the business of receiving and paying deposits of money within this state. A branch or office of any such bank shall be deemed a bank for the purpose of this act.

(b) The term "item" means any check, note or other instrument providing for the payment of money.

Agency Relationship to Depositor of Collecting Banks.

Section 2. Except as otherwise provided by agreement and except as to subsequent holders of a negotiable instrument payable to bearer or indorsed specially or in blank, where an item is deposited or received for collection, the bank of deposit shall be agent of the depositor for its collection and each subsequent collecting bank shall be subagent of the depositor but shall be authorized to follow the instructions of its immediate forwarding bank and any credit given by any such agent or subagent bank therefor shall be revocable until such time as the proceeds are received in actual money or an unconditional credit given on the books of another bank, which such agent has requested or accepted. Where any such bank allows any

revocable credit for an item to be withdrawn, such agency relation shall nevertheless continue except the bank shall have all the rights of an owner thereof against prior and subsequent parties to the extent of the amount withdrawn."

* * * * *

Section 4. (This section construes endorsements so as not to alter agency relations.)

* * * * *

"What May be Received in Payment Without Responsibility.

Section 9. Where ordinary care is exercised, any agent collecting bank may receive in payment of an item without becoming responsible as debtor therefor, whether presented by mail, through the clearing house or over the counter of the drawee or payor, in lieu of money, either (a) the check or draft of the drawee or payor upon another bank or (b) the check or draft of any other bank upon any bank other than the drawee or payor of the item or (c) such method of settlement as may be customary in a local clearing house or between clearing banks or otherwise: Provided, That whenever such agent collecting bank shall request or accept in payment an unconditional credit which has been given to it on the books of the drawee or payor or on the books of any other bank, such agent collecting bank shall become debtor for such item and shall be responsible therefor as if the proceeds were actually received by it in money.

Acceptance of Settlement from Subsequent Bank in Chain.

Section 10. Where ordinary care is exercised, any agent collecting bank may receive from any subsequent bank in the chain of collection in remittance for an item which has been paid, in lieu of money, the check or draft of the remitting bank upon any bank other than itself or the drawee or payor of the item or such other method of settlement as may be customary: Provided, That whenever such agent collecting bank shall request or accept an unconditional credit which has been given to it on the books of the remitting bank or on the books of any other bank, such agent collecting bank shall become debtor for such item and shall be responsible therefor as if the proceeds were actually received by it in money."

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934.

No. 338.

DAVID H. JENNINGS, RECEIVER OF THE NATIONAL BANK OF AMERICA, AND NATIONAL BANK OF AMERICA,
Petitioners,

v.

UNITED STATES FIDELITY AND GUARANTY COMPANY,
Respondent.

SUPPLEMENTAL BRIEF BY RESPONDENT.

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SUPPLEMENTAL BRIEF BY RESPONDENT.

FOREWORD.

Since Respondent's brief opposing certiorari was filed the Comptroller of the Currency filed a brief, *amicus curiae*, urging a decision on "the tracing of funds issues of law involved," regardless of outcome, and certiorari was granted.

This supplemental brief with Respondent's original brief will constitute its brief on the merits. The present brief goes chiefly to the Comptroller's brief.

SUMMARY OF ARGUMENT.

PROPOSITION I.

The proceeds received by the agent bank in payment for Respondent's item augmented the cash funds of the bank, and, as a part of such cash funds, they are traced into the cash funds now held by the Receiver.

Point 1.

The Comptroller's statement (p. 4) that no part of the cash funds in the Receiver's hands came to the bank from the collection transaction in question is erroneous. The statement completely ignores the fact that the item was collected by the bank as Respondent's agent in strict conformity with the agency authority conferred in Sec. 9 of the Indiana Uniform Bank Collection Code of 1929, and that under the terms of said Sec. 9 the agent bank received "in payment" for the item "proceeds" which to the bank were the equivalent of money and for which it did not become a debtor to Respondent.

> Secs. 3861.2, 3861.9, Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp. (In Appendix to first brief.)

The parties had not contracted otherwise (R. 18-21) and it is, therefore, presumed that they dealt with respect to the applicable state statute. *Federal Reserve Bank v. Malloy*, 264 U. S. 160, 164. Such commercial transactions engaged in by National banks are

controlled by state law. *Dakin v. Bayly*, 54 Sup. Ct. Rep. 113, 114, 115; *McClellan v. Chipman*, 164 U. S. 347, 356, 357; *Lewis v. Fidelity and Deposit Company*, 54 Sup. Ct. Rep. 848, 851.

Point 2.

The agent bank's cash funds were *augmented* by the exact amount of the proceeds collected by it on Respondent's item. Under express authority of said Sec. 9 the agent bank collected the item through the Gary clearing house and received "in payment," without becoming debtor therefor, certain checks drawn upon itself (a form of payment authorized by Sec. 9), in the total amount of which were involved the original form of the proceeds from the item collected. Such proceeds forming a part of the checks received in exchange were the same as cash to the agent bank, and it is stipulated and found (R. 23) that but for receipt of these exchanged checks the bank would that day have paid to the clearing house the exact amount of Respondent's item more than it actually did pay. The legal effect of the transaction was that the agent bank had received "in payment" for Respondent's item the full amount in a form expressly authorized by said Sec. 9, and that as a result the bank had exactly $2,196.89 more in its cash funds than it would otherwise have had. When such is the result there is true augmentation.

Ellerbe v. Studebaker Corporation of America, (4 C. C. A.) 21 Fed. (2d) 993, 997.

Point 3.

Means exist in the facts for ascertainment of the *trust res*, in substituted form, in the hands of the Receiver.

The item in collection was the original *trust res.* The next form of the *res* is found in the exchanged checks which, to the amount of Respondent's item, had been received "in payment" by the agent bank. A necessary result of the charging by the agent bank of the exchanged checks to the accounts of the drawers, in view of the continued agency relationship under Sec. 9, was that in legal effect an equivalent amount of the bank's cash funds became immediately substituted for the *trust res* which had been embodied in the total amount of the exchanged checks. Thus, the *trust res*, in altered form, is located in the total of the cash funds of the bank. Under Sec. 9, the bank remained a fiduciary as to $2,196.89 of the cash funds in its possession.

Only a half business day intervened between the day of collection, Dec. 31, 1931 (R. 23), and the day of the bank's suspension, Jan. 4, 1932 (R. 17). The total of said cash funds never receded below the trust fund of $2,196.89 after the collection was made, and the cash funds now in the Receiver's hands exceed that sum (R. 26).

The presumption is that the bank kept sacred the trust fund involved in its total cash funds, and that any payments it may have made in the brief time remaining before suspension (none shown) would have been made out of that part of the total of its cash funds which was unrestricted.

Schumacher v. Harriett, (4 C. C. A.) 52 Fed. (2d) 817, 818, 819;
Central National Bank v. Insurance Co., 104 U. S. 54, 68.

PROPOSITION II.

The *trust res*, in altered form, having been ascertained as constituting a part of the total cash funds now in the Receiver's possession, equity will separate it *in amount* and order it paid to its rightful owner.

Schumacher v. Harriett, (4 C. C. A.) 52 Fed. (2d) 817, 818, 819;
Central National Bank v. Insurance Co., 104 U. S. 54, 69;
Conf. St. Louis & S. F. R. R. v. Spiller, 274 U. S. 304, 309, 310.

PROPOSITION III.

The Comptroller's statement (p. 4) that Respondent's claim is given a "preferred status," whereas in the other circuits it would have a "general claim status" is incorrect.

Point 1.

The decision does not give Respondent a preference claim upon assets of the bank. The theory of the opinion and decision is that what is awarded to Respondent rightfully belongs to it and is not rightfully an asset of the bank, and the opinion expressly so says (R. 50).

Point 2.

No claim bottomed on a collection transaction made pursuant to the provisions of Sec. 9 of the Uniform Bank Collection Code, as is Respondent's, has been passed on by the courts of other circuits in any

of the cases cited by the Comptroller, and we can find none. It is, therefore, incorrect to say what the status of such a claim would be in other circuits.

PROPOSITION IV.

The Comptroller's statement (p. 4) that the decision in this case is contrary to the intent of the National Banking Act that liquidation of national banks be uniform throughout the United States, is incorrect.

Point 1.

This Honorable Court long ago said that the requirement as to ratable dividends is to make them from what belongs to the bank. *Scott v. Armstrong*, 146 U. S. 499, 510. Also, that the Act does not assume to appropriate trust funds, and that state courts have jurisdiction to determine whether particular funds are trust funds. *Capital Bank v. Cadiz Bank*, 172 U. S. 425, 433.

The instant decision is in harmony with the foregoing interpretation of the Act.

Point 2.

The results of the application of the identification rule must necessarily vary with the varying facts and relevant considerations in the cases where the rule is applied. And one such relevant consideration affecting the result may be the effect of such statutory provisions as are contained in Sec. 9 of the Uniform Bank Collection Code.

Recent decisions of this Honorable Court recognize permissible divergency in results in the liquidation of insolvent National banks as dependent on applicable provisions of state statutes. Compare, *Lewis v. Fidelity and Deposit Company*, 54 Sup. Ct. Rep. 848, and *City of Marion v. Ben Sneeden*, 78 Law Ed. 521.

PROPOSITION V.

The decision does not conflict with principles of law decided in the cases of this Court which the Comptroller cites. These will be examined in the argument.

PROPOSITION VI.

The opinion and decree properly rest on findings showing an identified *trust res* in possession of the Receiver. The decree would, however, be right without such identification in view of the trust which is impressed on the agent bank's assets by paragraph 3 of Sec. 13 of the statute under which the collection was made, regardless of whether the funds representing the proceeds can be traced and identified.

Sec. 3861.13 (3), Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp., see Appendix hereto.

ARGUMENT

OF PROPOSITIONS I AND II (pp. 2, 5).

The Comptroller erred (p. 4) in saying that the decision went for Respondent "despite record proof that not one penny of such funds actually came into the bank from claimants' transaction." The Comptroller ignores the effect of an applicable state statute.

The Uniform Bank Collection Code was in force in Indiana when this collection was made (Sec. 3861.1-19, Vol. IV, Burns' Ann. Ind. Stat., 1929 Supp.).

The parties had not contracted differently from the provisions of said statute, and the presumption is that the parties contracted with reference to that statute. *Federal Reserve Bank v. Malloy*, 264 U. S. 160, 164. In virtue of Sec. 2 of said statute, National Bank of America became Respondent's subagent. The bank was an agent collecting bank within the meaning of Sec. 9 of said statute, and it made the collection of Respondent's item as such agent within the scope of the agency authority conferred on it in Sec. 9.

As a matter of general law such subagent bank would have had agency authority to receive only legal tender money in payment for the item. *Federal Reserve Bank v. Malloy*, 264 U. S. 160, 165.

But Sec. 9 of said statute authorized this agent collecting bank, acting as Respondent's subagent, to receive "in payment" for the item, in lieu of money, and without becoming responsible as debtor therefor, whether presented by mail, through the clearing house or over the counter of the drawee or payor, "either

(a) the check or draft of the drawee or payor upon another bank or (b) the check or draft of any other bank upon any bank other than the drawee or payor of the item or (c) *such method of settlement as may be customary in a local clearing house or between clearing banks or otherwise.*"

Payment was received by the agent bank for Respondent's item in a manner and form authorized under (c), *viz:* upon presentment of the item to the drawee bank through the Gary clearing house, the agent bank received in exchange checks totalling $11,470.19, drawn upon itself (R. 23).

Authorized payments in forms other than money are characterized as "proceeds" in a proviso to Sec. 9. Said proviso makes the agent bank a debtor if it requests or accepts in payment an unconditional credit which has been given to it on the books of the drawee or payor or on the books of any other bank. Otherwise, the proviso is here immaterial, for the conditions under which the agent bank would become a debtor did not exist.

Under the facts, and in virtue of said Sec. 9, the agent bank received *payment* for Respondent's item in the form of checks drawn upon itself and the proceeds from Respondent's item were, in their first form, involved in these exchanged checks, with the agency relationship still continuing. Sec. 9, of course, contemplated that if payment were received in the form of such checks that the agent bank might charge them against the drawers' accounts while it still remained such agent and while it still remained under a fiducial duty to remit the proceeds which it received "in payment." It follows, that upon the charging of such

checks to the accounts of the drawers a legal substitution of an equivalent amount of the agent bank's cash and cash items occurred for the proceeds which had been involved in the total of said checks, and that the agent bank remained a fiduciary in respect to the substituted form of the *trust res.* What the agent bank had received "in payment" for Respondent's item was the same as cash to it and became immediately reflected in its remaining cash and cash items.

This is not a case of a bank having left more cash and cash items on hand after a clearing house transaction as a result of the misuse of an item in collection to pay the agent bank's own debts in violation of the agency authority. This is a case where the agent bank *collected* the item in strict conformity with the agency authority conferred on it in said Sec. 9, and as a result of which it received "in payment" for Respondent's item the full amount. The effect is clearly such that as a result of such payment the agent's cash and cash items were augmented by that exact amount. Indeed, it is stipulated and found by the Court (R. 23) that but for this collection transaction the agent bank would have paid to the clearing house the exact amount of Respondent's item more than it did pay.

The provisions of Sec. 9 of said Code in no wise impaired the functions of the bank as a government agency and they were not in conflict with any Federal law, and they clearly applied to and controlled the transaction. *Lewis v. Fidelity and Deposit Company,* 54 Sup. Ct. Rep. 848, 851; *McClellan v. Chipman,* 164 U. S. 347, 356, 357; *Federal Reserve Bank v. Malloy,* 264 U. S. 160, 164.

When the true nature of the transaction and its legal consequences under said Sec. 9 are regarded, it

becomes plain that the cash and cash items of the agent bank were truly augmented by the exact amount of the proceeds from Respondent's item.

Such augmentation established, the proceeds of Respondent's item as first involved in the total amount of the exchanged checks are, under the principle of substitution above stated, in altered form clearly traced into the total of the agent's cash and cash items remaining after the clearing house transaction of December 31, 1931, which was the next to the last day the bank did business.

The bank's cash and cash items never receded below the amount of Respondent's item and the funds now in the Receiver's hands are in excess of that amount.

What the agent bank may have paid out during the less than a day and a half while it remained open for business after this collection was made (nothing shown) would presumptively have been paid out of the unrestricted portion of its funds. *Peoples Nat. Bank v. Moore*, (8 C. C. A.) 25 Fed. (2d) 599, 601; *Central National Bank v. Insurance Co.*, 104 U. S. 54, 68.

In these circumstances, under the modern rule governing tracing, the proceeds of Respondent's item, in altered form, are sufficiently ascertained as constituting a part of the cash funds in the Receiver's hands, and equity will order their separation and payment to Respondent as the rightful owner thereof. *Schumacher v. Harriett*, (4 C. C. A.) 52 Fed. (2d) 817, 818, 819; *Central National Bank v. Insurance Co.*, 104 U. S. 54, 69; *St. Louis & S. F. R. R. v. Spiller*, 274 U. S. 304, 309, 310.

OF PROPOSITION III (p. 5).

Respondent's claim is not given a "preferred status" in the sense that a preferred claim upon assets is allowed. The opinion expressly says (R. 50) that "The proceeds of appellee's check were not rightfully a part of its assets, and there is no effort here to secure a preference over any creditor in the distribution of the assets."

Neither was it correct for the Comptroller to say (p. 4) that such a claim, bottomed in part on applicable provisions of the Uniform Bank Collection Code as is Respondent's, has only the status of a general creditor claim in other jurisdictons. He cites no case, and we know of none, involving a claim thus bottomed that any other court has ever passed upon. What the courts in other circuits would hold in such a case is not known because they have not yet spoken.

The Comptroller overlooks the proposition that as a matter of general law a bank entrusted with an item for collection and remittance has agency authority only to receive legal tender money in payment. *Federal Reserve Bank v. Malloy*, 264 U. S. 160, 165. He also overlooks the distinction between a transaction where only the general law obtains and a bank, in violation of its trust, *converts* an item by using it in a clearing transaction for the purpose of paying its own debts, as in *Farmers Nat. Bank v. Pribble*, 15 Fed. (2d) 175, and a transaction, such as the instant one, where an agent bank acting strictly within its agency authority conferred by statute *collects* the item and receives something "in payment."

In the one instance the result is merely to decrease indebtedness by the wrongful use of the item held in

trust, while in the other instance the legal effect is that the agent bank actually receives proceeds in payment. In the one case the basis for augmentation is usually lacking, while in the other instance there is clearly augmentation by the amount received in payment whatever its form. And in the instant case, the form of the proceeds were such as to find immediate affirmative reflection in the agent bank's cash and cash items.

The Comptroller also overlooks the distinction between the instant transaction as governed by Sec. 9 of the Uniform Bank Collection Code and in which proceeds from the collection came to the agent bank from another bank and transactions governed by general law where the collecting banks were also the paying banks and a mere shifting of credits occurred, as in *City of Miami v. First National Bank*, 69 Fed. (2d) 346; *Allied Mills v. Horton*, 65 Fed. (2d) 708; *Larabee Flour Mills v. First National Bank*, 13 Fed. (2d) 330, and in other cases he cites.

Respondent contends that all decisions of other circuits cited, and which could be cited, rest on considerations of general law and not upon the practical legal effects imputed by Sec. 9 of the Bank Collection Code, and that under the facts and the law in the instant case the decision is correct.

OF PROPOSITION IV (p. 6).

No intent of the National Banking Act as to uniformity of liquidation of banks is violated by the instant decision. Ascertainable trust funds always go to the rightful owner, *Capital Bank v. Cadiz Bank*, 172 U. S. 425, 433, and only that which rightfully

belongs to the bank goes to creditors. *Scott v. Armstrong*, 146 U. S. 499, 510.

The results of the application of the rule that a *trust res* must be identified by its claimant either in original or altered form must, of course, depend on the particular facts and considerations in the case where the rule is applied.

Relevant considerations affecting the result of application of the identification rule in a particular case may, as here, be of the provisions of a State Uniform Bank Collection Code pursuant to which an agent collecting bank made the collection and received something "in payment" for the item. And if such considerations dictate a different result from what the result would be where the Code does not obtain and where the construction under general law would be that the bank entrusted with an item for collection violated its agency authority and misused the item for the purpose of paying its own debts, such divergency in results of the application of the identification rule would not violate any intent of the National Banking Act.

Occurrence of divergent results in different jurisdictions in the liquidation of insolvent National banks as dependent on state statutes is recognized in two cases recently decided by this Honorable Court. Thus, in *Lewis v. Fidelity and Deposit Company*, 54 Sup. Ct. Rep. 848, it was held that Georgia had a lien for state deposits on the assets of a failed National bank in view of certain provisions of a statute of that state; whereas Illinois, under similar facts, did not have such a lien because its depository

statute did not go so far as that of Georgia. *City of Marion v. Ben Sneeden*, 78 Law Ed. 521.

OF PROPOSITION V (p. 7).

The instant decision conflicts with nothing decided in *Schuyler v. Littlefield*, 232 U. S. 707, 713. The principle that trust funds may be recovered if satisfactorily traced is recognized but the requisite proof was not there present.

The rule stated in Note 19 to the opinion in *Pottorff v. Texas & Pacific R. Co.*, 291 U. S. 245, is not violated here, but is, indeed, complied with. The rule there stated is that "The claimant has the burden of identifying the property in its original or altered form." The opinion in the instant case expressly says the same thing in effect (R. 50).

In *Davis v. Elmira Savings Bank*, 161 U. S. 275, a New York state statute was held ineffective because it did not profess to deal with the bank and its relations as a going concern, but it "wholly and exclusively undertakes to regulate the distribution of assets after insolvency." The first twelve sections of the Uniform Bank Collection Code deal exclusively with banks as *going concerns*, and under the rule expressly recognized in the *Davis* case (p. 287) those sections do control the collection transactions of National banks as going concerns and operate to fix relations at the moment when suspension occurs.

The reference by the Comptroller to *Cook County National Bank v. United States*, 107 U. S. 445, 448, merely shows that the winding up of National banks is controlled by Federal statute. The instant decision is not in conflict with that principle.

OF PROPOSITION VI (p. 7).

Respondent's position, heretofore stated, is that a *trust res* of which it is the beneficial owner has been identified in the Receiver's possession. The decision under review is properly put on that ground by the opinion of the Circuit Court of Appeals.

But the decree would be right without such identification established in view of the trust which is impressed on the agent bank's assets by paragraph 3 of Sec. 13 of the statute under which the collection was made, regardless of whether the funds representing the proceeds can be traced and identified.

That paragraph of Sec. 13 (p. 20, Appendix hereto) impresses a trust on the assets of a failed non-debtor agent bank in favor of its principal for the amount of unremitted proceeds of a collected item, irrespective of whether the funds representing such item can be traced and identified as a part of such assets or has been intermingled with or converted into other assets of such failed bank, and the paragraph also provides that the principal shall have a preferred claim upon the assets so impressed.

Properly understood, the provisions in paragraph 3 of Sec. 13 are not in conflict with Federal law governing distribution of assets. These provisions do not deal with creditor interests and they apply only where the agent bank, as here, is not responsible as debtor for the proceeds of the collected item. The trust which is impressed is the same trust which arises under the provisions of Sec. 9 of the same statute at a time when the agent bank is a going concern. The provision for a "preferred claim" is not an effort to prefer a creditor out of anything belonging beneficially to the bank, but is merely a device adopted to secure to the principal

something which from the beginning is beneficially his. Hence, there is no conflict with the Federal law governing distribution of that which beneficially belongs to the bank.

Nor should equity have any difficulty here. These provisions go only one step farther than equity has gone in the absence of such agency authority as Sec. 9 confers for receiving payments in transmutable forms which can frequently not be traced and identified. That step is to secure to the beneficial owner the amount of collected proceeds, irrespective of tracing and identification of the fund representing such proceeds. This is a permissible step in view of the new step taken in Sec. 9 by which the agent may receive for the principal proceeds of transmutable type but which are none the less real in modern banking methods. Both steps taken by this statute are in recognition of modern business methods in such collection transactions. The step taken in Sec. 9 will, of course, be allowed, and the one taken in paragraph 3 of Sec. 13 ought also be allowed. The same power which gives the agent bank its exclusive authority to receive proceeds of that character without becoming responsible as debtor therefor ought also be able to make effective provisions in the same statute for effective preservation to the principal of the beneficial interest to such proceeds regardless of their transmutations.

The history of the court-made tracing and identification rule has itself been one of progressive adaptation to changing methods of doing business. The rigors of the original rule have become much relaxed, and earmarks are no longer required. Equity, always concerning itself more with substance than with form,

should find no difficulty in allowing the step taken in paragraph 3 of Sec. 13 in cases where, as here, the step is intended to apply. To do so only requires application of the maxim that equity follows the law.

Receipt of proceeds by a national agent bank under exclusive authority of Sec. 9 of the Uniform Bank Collection Code necessarily implies submission by the bank to the trust provisions contained in the statute. In effect there is an equitable lien provided in favor of the principal for the amount of the proceeds collected by the agent bank. The principle is established that where a National bank voluntarily enters into a permissible transaction which is governed by a state law which demands a lien on the bank's assets, such lien will be respected in liquidation proceedings. *Lewis v. Fidelity and Deposit Company*, 54 Sup. Ct. Rep. 848.

The validity of the argument that paragraph 3 of Sec. 13 should be given application is not impaired by the fact that in jurisdictions where the Uniform Bank Collection Code is not yet in force the tracing and identification rule must be observed. In those jurisdictions general law limits agency authority to the collection and remittance of legal tender money. The presumption is that these limitations will be observed in those jurisdictions, and if an agent bank violates the limitation and becomes trustee *ex maleficio* that would afford sufficient distinction for results in jurisdictions where such is the case different from what the results should be where the agent bank performs lawfully and becomes trustee under the statute giving the authority exercised.

It is respectfully submitted that an identifiable *trust res* has been ascertained in this case as constitut-

ing part of the total cash funds held by the Receiver and that the decision should be affirmed on that ground. If that view were not accepted, then the decision should be affirmed in virtue of the provisions in Sec. 13 of the Uniform Bank Collection Code.

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APPENDIX.

SECTION 13 OF UNIFORM BANK COLLECTION CODE, CH. 164, INDIANA ACTS OF 1929.

Procedure When Bank Fails or Is Closed for Business.

Sec. 13. (1) When the drawee or payor, or any other agent collecting bank shall fail or be closed for business by the state bank commissioner or by action of the board of directors or by other proper legal action, after an item shall be mailed or otherwise entrusted to it for collection or payment but before the actual collection or payment thereof, it shall be the duty of the receiver or other official in charge of its assets to return such item, if same is in his possession, to the forwarding or presenting bank with reasonable diligence.

(2) Except in cases where an item or items is treated as dishonored by nonpayment as provided in section 11, when a drawee or payor bank has presented to it for payment an item or items drawn upon or payable by or at such bank and at the time has on deposit to the credit of the maker or drawer an amount equal to such item or items and such drawee or payor shall fail or close for business as above, after having charged such item or items to the account of the maker or drawer thereof or otherwise discharged his liability thereon but without such item or items having been paid or settled for by the drawee or payor either in money or by an unconditional credit given on its books or on the books of any other bank, which has been requested or accepted so as to constitute such drawee or payor or other bank debtor therefor, the assets of

such drawee or payor shall be impressed with a trust in favor of the owner or owners of such item or items for the amount thereof, or for the balance payable upon a number of items which have been exchanged, and such owner or owners shall be entitled to a preferred claim upon such assets, irrespective of whether the fund representing such item or items can be traced and identified as part of such assets or has been intermingled with or converted into other assets of such failed bank.

(3) Where an agent collecting bank other than the drawee or payor shall fail or be closed for business as above, after having received in any form the proceeds of an item or items entrusted to it for collection, but without such item or items having been paid or remitted for by it either in money or by an unconditional credit given on its books or on the books of any other bank which has been requested or accepted so as to constitute such failed collecting or other bank debtor therefor, the assets of such agent collecting bank which has failed or been closed for business as above shall be impressed with a trust in favor of the owner or owners of such item or items for the amount of such proceeds and such owner or owners shall be entitled to a preferred claim upon such assets, irrespective of whether the fund representing such item or items can be traced and identified as part of such assets or has been intermingled with or converted into other assets of such failed bank.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. 338.

DAVID H. JENNINGS, Receiver of the National Bank of America, and NATIONAL BANK OF AMERICA, *Petitioners,*

vs.

UNITED STATES FIDELITY AND GUARANTY COMPANY, *Respondent.*

BRIEF OF THE COMPTROLLER OF THE CURRENCY AS AMICUS CURIAE.

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PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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DAVID H. JENNINGS, Receiver of the National Bank of America, and NATIONAL BANK OF AMERICA, *Petitioners*,

vs.

UNITED STATES FIDELITY AND GUARANTY COMPANY, *Respondent*.

BRIEF OF THE COMPTROLLER OF THE CURRENCY AS AMICUS CURIAE.

Comes now J. F. T. O'Connor, Comptroller of the Currency of the United States, and respectfully submits his brief, as amicus curiae, in support of the petition for writ of certiorari filed by David H. Jennings, Receiver of the National Bank of America of Gary, Indiana, in the above entitled cause.

I.

FOREWORD.

Citation of the opinions below, statement concerning the jurisdiction of the court to issue writ of certiorari, summary of the facts, specification of errors, and argument of the is-

sues involved, have been summarized in the petition for writ of certiorari and supporting brief filed by the Receiver of the National Bank of America, Gary, Indiana, and therefore reference is here made to the same in the interest of avoiding repetition.

II.

INTEREST OF THE COMPTROLLER OF THE CURRENCY IN THE CASE FROM AN ADMINISTRATIVE STANDPOINT.

The Comptroller of the Currency is now engaged in liquidating 1547 insolvent National banks,—the largest number in the history of the National Banking Act,—for the purpose of making ratable distribution to approximately three and one-half million depositors and other creditors owning claims against said banks at suspension amounting approximately to one billion eight hundred and fifty million dollars. Before disbursement can be made it is required that the claims, whether general or preferred, be established to the satisfaction of the Comptroller, or in a court of competent jurisdiction. (Sections 5234, 5235, 5236 U. S. R. S.; U. S. C., Ch. 2, Title 12, Sections 192, 193, 194.)

Thousands of preferred claims have been asserted before the Comptroller incident to the liquidation of these banks. Such preferred claims are allowed by the Comptroller where it affirmatively appears, as required by the rule settled by weight of authority in the Federal courts, that the bank received an identifiable res in trust for the claimant and the proceeds are traceable into the hands of the bank Receiver. *Larabee Flour Mills v. First National Bank* (C. C. A. 8), 13 Fed. (2nd) 330-331, certiorari denied 273 U. S. 727; *City of Miami v. First National Bank* (C. C. A. 5), 69 Fed. (2nd) 346, 349; *Allied Mills v. Horton*, 65 Fed. (2nd) 708; *Board of Commissioners v. Strawn* (C. C. A. 6), 157 Fed. 49, 54. The Comptroller's disallowance of such claims, where found invalid, has resulted in the filing of many ac-

tions now pending in the United States District Courts and Circuit Courts of Appeal. To quote the opening sentence from the recent opinion of the Circuit Court of Appeals for the Fifth Circuit in *Wisdom v. Keen*, 69 Fed. (2nd) 349:

> "This is another of the multiplying cases in which the ratable distribution to all creditors of the assets of a failed National bank under 12 U. S. C. A., Sec. 194, is sought to be disturbed by the assertion of a lien upon them because of a commingled trust fund."

While there have been hundreds of decisions of United States District Courts and Circuit Courts of Appeal, disposing of such claims, we find only one case of preferred claim against a national bank in receivership that has been reviewed on the merits by this court, that of *Blakey v. Brinson*, 286 U. S. 254. This Court's decision in the Blakey case turned on the trust relationship question exclusively, and consequently this Court has never directly passed upon the tracing of funds feature of these claims against insolvent National banks, which factor is controlling in most instances.

The instant case turns upon the tracing of funds feature and involves the factual situation common to this type of cases. The now closed bank received a check in the amount of $2196.89 for collection and remittance and effected collection in the customary way through a clearing house transaction which resulted in a debit balance against it. Such a transaction neither augmented the now closed bank's assets nor permitted tracing to the Receiver, within the purview of the requirements established by the Circuit Court of Appeals, Eighth Circuit, in *Farmers National Bank v. Pribble*, 15 Fed. (2nd) 175, and the many other Federal cases some of which are cited page 2, *supra*. The Court below undertakes to avoid this rule, apparently by a finding that an Indiana statute, the Uniform Bank Collection Code, imputes augmentation and tracing, despite the record to the contrary, and also by a finding that the bank's

cash that passed to the Receiver was greater by the sum of $2196.89 because of the use of the claimant's item in the clearings, in lieu of the bank's cash, which is in conflict with the following rule of the Pribble case quoted from page 176 of the opinion:

> "The fact that the claimant's property paid or reduced the indebtedness or liability of the insolvent corporation so that it will pay a larger percentage of its debts justifies no lien on its assets by or preference in payment to the cestui que trust."

The court below thus holds that the funds in the hands of the bank Receiver belonging to depositors, whose equities, we submit, are at least equal to those of the claimant, shall respond *in full* for the trust claim of $2196.89, despite record proof that not one penny of such funds actually came into the bank from the claimant's transaction.

As the result of this decision, a claim of this character,—and there are many such claims,—has a preferred status against an insolvent National bank located in the Seventh Circuit, but has a general claim status only, in the other Circuits, contrary, we submit, to the intent of the National Banking Act which contemplates a plan of liquidation that will be uniform throughout the 48 States. Cook County National Bank v. United States, 107 U. S. 445, 448; *First National Bank v. Selden*, 120 Fed. 212, 215. The decision in the instant case appears to be in *direct conflict* with the principles of law heretofore applied in the Circuits other than the Seventh, and with the principles applied and stated by this Court in *Schuyler v. Littlefield*, 232 U. S. 707, 713, and *Pottorff v. Texas & Pacific Railroad Co.*, 291 U. S. 245, 261, Note 19. The instant case is the first decision of an Appellate Federal Court holding that a State statute [illegible]he Uniform Bank Collection Code), can increase or affect in any way the rights of a trust claimant against an insolvent National bank, and it appears to be contrary in principle to the decisions of this court in *Davis v. Elmira Savings*

Bank, 161 U. S. 275, 287; *Easton v. Iowa*, 188 U. S. 220, 231, and *Cook County National Bank v. United States*, 107 U. S. 445, 448. The Uniform Bank Collection Code has been adopted in 18 States, including New York, Pennsylvania, Illinois, Indiana, Michigan and New Jersey; consequently this phase of the decision of the court below is of class importance in the winding up of National banks, and to banking and business interests generally.

Every effort is being made by the appropriate Federal agencies to give speedy relief to the depositors and creditors of insolvent National banks. A decision by this court settling the tracing of funds issues of law involved in the instant case and the companion case of *Adams v. Champion*, now pending in this court on petition for writ of certiorari, No. this term,—regardless of whether the decisions below be affirmed or reversed,—will be of inestimable aid to the Comptroller in disposing of the large number of similar pending claims and will unquestionably substantially expedite the liquidation of National banks in Receivership by making possible the disposition of numerous other actions pending in the Federal courts involving the same issues, and by eliminating future litigation of the same type.

III.

CONCLUSION.

The Comptroller of the Currency therefore earnestly urges this Honorable Court to entertain the petition for write of certiorari filed by the Receiver in the instant case.

Respectfully submitted,

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2 4

SUPREME COURT OF THE UNITED STATES.

No. 338.—October Term, 1934.

David H. Jennings, Receiver of the National Bank of America, and National Bank of America, Petitioners, *vs.* United States Fidelity and Guaranty Company, Respondent.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

[February 4, 1935.]

Mr. Justice Cardozo delivered the opinion of the Court.

A trust has been impressed upon the assets of a national bank in the hands of a receiver for the proceeds of a check collected through a clearing house before the closing of the bank by the Comptroller of the Currency. The question is whether the trust may be upheld.

On December 29, 1931, the Commercial Trust Company of Gary, Indiana, as maker, delivered to the respondent, United States Fidelity and Guaranty Company, a check to the order of respondent in the sum of $2,196.89 upon the Gary State Bank of Gary, Indiana, as drawee. The check, duly endorsed by the payee, was deposited in a bank in Indianapolis, and thereafter was transmitted for collection to the National Bank of America at Gary, Indiana, being received for that purpose on December 31, 1931. At that time both the collecting bank (the National Bank of America) and the drawee bank (Gary State Bank) were members of the Gary Clearing House Association. In accordance with banking custom the National Bank of America delivered to the local clearing house whatever checks in its possession were payable by the member banks (a total of $10,425.45) including the foregoing item of $2,196.89, and received in return the checks drawn on itself ($11,470.19). The outcome was a debit balance of $1,044.74, which it paid on the same day by a draft, thereafter duly honored, to the order of the clearing house. At the same time it delivered to the forwarding bank in Indianapolis a draft for $3,660.83, which

covered along with other items the check for $2,196.89, collected from the drawee in the manner just described. Before the draft so transmitted could be honored, its maker, the collecting bank, had been forced to close its doors (January 4, 1932), and the Comptroller of the Currency was in possession of the business.

This action which was begun in a state court in Indiana and was thereupon removed to a United States District Court, was brought by the United States Fidelity and Guaranty Company, payee of the check for $2,196.89, against the collecting bank and Jennings, its receiver, to impress a trust upon the assets to the extent of the proceeds of collection, and for payment accordingly. The District Court held that the payee was entitled to a preference over the general creditors of the insolvent bank, and entered a decree for the face amount of the check with interest. 4 F. Supp. 569. Upon appeal to the Circuit Court of Appeals for the Seventh Circuit, the decree was modified as to the interest, and as modified affirmed. 71 F. (2d) 618. A writ of certiorari brings the case here.

There was in force in Indiana in 1931 a statute known as the Bank Collection Code (Indiana Acts, 1929, c. 164[1]), which is applicable to national banks in so far as it is consistent with the policy or provisions, express or reasonably implied, of the National Bank Act or of other federal acts of paramount authority. *Lewis* v. *Fidelity & Deposit Co. of Maryland,* 292 U. S. 559, 566; *First National Bank* v. *Missouri,* 263 U. S. 640, 656. Under that code (§ 2), the relation between the forwarding bank and the collecting bank is that of principal and agent until the agent has completed the business of collection. Whether a fiduciary relation continues even afterwards, upon the theory that the proceeds of the collection until remitted to the forwarder are subject to a trust, depends upon the circumstances. In the absence of tokens of a contrary intention, the better doctrine is, where the common law prevails, that the agency of the collecting bank is brought to an end by the collection of the paper, the bank from then on being in the position of a debtor, with liberty, like debtors generally, to use the proceeds as its own. *Commercial Bank of Pennsylvania* v.

[1]The Code is stated to have been adopted in as many as eighteen states. It was framed by counsel for the American Bankers Association in an endeavor to promote uniformity of banking practice in the collection of commercial paper.

Armstrong, 148 U. S. 50; *Marine Bank* v. *Fulton Bank,* 2 Wall. 252; *Planters' Bank* v. *Union Bank,* 16 Wall. 483, 501; *Hecker-Jones-Jewell Milling Co.* v. *Cosmopolitan Trust Co.,* 242 Mass. 181, 185, 186; *Freeman's National Bank* v. *National Tube Works Co.,* 151 Mass. 413, 418; *Manufacturers National Bank* v. *Continental Bank,* 148 Mass. 553, 558; *First National Bank of Richmond* v. *Wilmington & W. R. Co.,* 77 Fed. 401, 402; *Philadelphia National Bank* v. *Dowd,* 38 Fed. 172, 183; *Merchants' Bank* v. *Austin,* 48 Fed. 25, 32.[2] "One who collects commercial paper through the agency of banks must be held impliedly to contract that the business may be done according to their well known usages, so far as to permit the money collected to be mingled with funds of the collecting bank." *Freeman's National Bank* v. *National Tube Works Co., supra.* There is a contention for the respondent that the rule at common law has been modified by statute. We shall consider later on whether the change, if any, is material upon the record now before us.

At the closing of its doors on January 4, 1932, the collecting bank at Gary had finished the business of collection, and had arrived at the stage when it was subject to a duty, either as trustee or as debtor, to make remittance of the proceeds. In the method of collection there had been no departure from the ruling of this court in *Federal Reserve Bank* v. *Malloy,* 264 U. S. 160, that an agent bank is at fault when it accepts anything but cash in the absence of custom or agreement for the acceptance of a substitute. To preclude the extension of that ruling to collections through a clearing house the Bank Collection Code makes provision in § 9 for media of payment that are to be deemed equivalent to currency. There may now be acceptance of a bank draft, or settlement through a clearing house in the customary manner, without involving the agent in liability for damages if the draft is dishonored or the credit subsequently revoked.[3] On the other hand, when

[2]The decisions to the contrary are criticized in Hecker-Jones-Jewell Co. *v.* Cosmopolitan Trust Co., *supra,* and additional decisions are collected by Scott, Cases on Trusts, pp. 67, 68.

[3]§ 9. "Where ordinary care is exercised, any agent collecting bank may receive in payment of an item without becoming responsible as debtor therefor, whether presented by mail, through the clearing house or over the counter of the drawee or payor, in lieu of money, either (a) the check or draft of the drawee or payor upon another bank of (b) the check or draft of any other

credit ceases to be provisional, or when the accepted instrument is paid, the collecting bank is liable as debtor, if not otherwise, to the same extent as if payment had been made in cash over the counter. One duty—the duty to collect—is at an end, and another —the duty to remit—has arisen in its place.

To say that a collecting agent may be held to the liability of a debtor "as if" payment had been made in cash is not to say that the two methods of collection are equivalent for every other purpose. More particularly it does not mean that they are equivalent for the purpose of identifying a *res* to be subjected to a trust. The distinction is made definite by the controversy before us. What happened in the clearing house was this, that a check for $2,196.89, due to the collecting bank as agent or fiduciary, was used to cancel or extinguish liability upon a check or checks of equal amount due from it as principal, all with the sanction of statute and with the tacit assent of the forwarder or owner. At the close of the day there was not a dollar in the treasury of the agent that could be identified as part of the proceeds of collection or as a substitute therefor. If the money had been paid over the counter with the understanding that it was accepted as a special deposit (*Blakey* v. *Brinson,* 286 U. S. 254, 262, 263; *People* v. *City Bank of Rochester,* 96 N. Y. 32; *Genesee Wesleyan Seminary* v. *United States Fidelity & Guaranty Co.,* 247 N. Y. 52, 55), the doctrine of a continuing trust would charge the agent with a duty to set the proceeds of collection apart from other assets, and hold them intact for transmission to the forwarder. Nothing of the

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bank upon any bank other than the drawee or payor of the item or (c) such method of settlement as may be customary in a local clearing house or between clearing banks or otherwise: *Provided,* That whenever such agent collecting bank shall request or accept in payment an unconditional credit which has been given to it on the books of the drawee or payor or on the books of any other bank, such agent collecting bank shall become debtor for such item and shall be responsible therefor as if the proceeds were actually received by it in money."

The time within which credit, when once given, may be revoked is defined by § 3: "A credit given by a bank for an item drawn on or payable at such bank shall be provisional, subject to revocation at or before the end of the day on which the item is deposited in the event the item is found not payable for any reason. Whenever a credit is given for an item deposited after banking hours such right of revocation may be exercised during the following business day."

kind was done. Nothing of the kind was required or expected to be done. On the contrary, the statute gave notice to the agent that instead of establishing a trust, it was at liberty to set off what was due to it in one capacity against what was owing by it in another, being liable, however, as debtor when the set off became final.

We are not concerned at this time with a constructive trust in the strict sense, a trust *ex maleficio*, which may be fastened upon a wrongdoer irrespective of intention. Pomeroy, Equity Jurisprudence, vol. 1, § 155; vol. 3, §§ 1044, 1046. There was no wrongdoing here, but conduct wholly regular, with the result that any trust existing must be one implied in fact. In that situation there is no basis for a holding that a trust was transferred from the proceeds of collection to an equivalent part of the cash resources of the agent, the beneficial interest of the principal being unaffected by the set off. Cf. *Knatchbull* v. *Hallett*, 13 Ch. Div. 696; *National Bank* v. *Insurance Co.*, 104 U. S. 54, 68; *Schuyler* v. *Littlefield*, 232 U. S. 707. To draw such an inference, far from promoting intention, would ignore and override it. By a permitted course of dealing the proceeds of the check, instead of being deposited upon collection in the vaults of the collecting agent, were specifically appropriated to the discharge of other obligations. There was not even a partial or proportionate payment that could have found its way into the vaults, for the balance at the close of the operations of the day was adverse to the collector and in favor of the clearing house. These being the facts, there is no room in our view for the use of those presumptions that affect the conduct of a wrongdoer who draws upon a mingled fund made up of his own moneys and another's. *Knatchbull* v. *Hallett, supra; National Bank* v. *Insurance Co., supra.* The presumption collapses when there is neither trust nor wrong.

For the purposes of this case we do not need to determine whether the Bank Collection Code has changed the preëxisting rule whereby in the absence of tokens of a contrary intention a bank ceases to be an agent and is turned into a debtor when collection is complete, without reference to the form or manner of the payment. If we assume for present purposes that a trust will attach under the statute when the proceeds of the collection are in the hands of the collector, the assumption will not hold where there are no proceeds of collection that have ever come into his

hands, or where such proceeds as there were have been so mingled and confused that it is impossible to follow them. Currency paid over the counter and deposited in a vault is a thing that can be identified and so subjected to a trust whenever in equity and conscience a trust should be implied. Not only that, but a trust so created will not fail though other dollars may have taken the place of those originally received, for dollars are fungibles and any one of them will be accepted as a substitute for another. *Knatchbull* v. *Hallett, supra.* But the situation is very different when what has been received by the collecting agent is not a thing at all, but a reduction of liabilities by set off or release. *Blakey* v. *Brinson, supra; People* v. *Merchants & Mechanics Bank,* 78 N. Y. 269, 272, 273; *Hecker-Jones-Jewell Milling Co.* v. *Cosmopolitan Trust Co., supra,* p. 187; *City Bank* v. *Blackmore,* 75 Fed. 771; *Anheuser-Busch Brewing Association* v. *Clayton,* 56 Fed. 759; *Farmers National Bank* v. *Pribble,* 15 F. (2d) 175, 176; *Dickson* v. *First National Bank,* 26 F. (2d) 411; *Schilling* v. *Rowe,* 64 F. (2d) 188, 190; *Allied Mills* v. *Horton,* 65 F. (2d) 708, 710; *Smith* v. *Zemurray,* 69 F. (2d) 5, 6, 7; *First National Bank of St. Petersburg* v. *City of Miami,* 69 F. (2d) 346; *Wisdom* v. *Keen,* 69 F. (2d) 349.[4] A debt does not furnish a continuum upon which a trust can be imposed after cancellation or extinguishment has put the debt out of existence.

The truth of this statement, though obvious enough upon its face, finds point and confirmation when the benefit, if any, accruing to the debtor is viewed as of the time of insolvency or later. What was done by the collecting bank through a settlement in the clearing house has not increased the assets available for distribution in the hands of the receiver. What was done through that settlement has had no effect after insolvency except to diminish liabilities. The dividend that would be due upon the debts canceled through the set off if they were now to be revived is the measure of any benefit accruing to the creditors. Decisions of other courts, to the extent that they give support for a different conclusion are built, as we think, upon an inadequate analysis, and do not win our approval.[5] It is the benefit to the creditors, not the

[4]Many cases are collected in Bogert, Failed Banks, Collection Items and Trust Preferences, 29 Mich. Law Review 545, 551, 552.

[5]For a collection of the cases, see 82 A. L. R. 97.

loss to the respondent, that marks the gain to the fund now held by the receiver. If the respondent is permitted to prove against the assets on a parity with other creditors, the share thus allotted will correspond accurately to whatever accretion has resulted from the act of set off and cancellation in the operations of the clearing house.

One other section of the Bank Collection Code is still to be considered. This is section 13, which has to do, as its caption indicates, with the procedure following insolvency. What is regulated in that section is not the relation between a bank and its correspondents during the normal course of business. What is regulated is the relation and the remedy when insolvency has set in and business is suspended.[6] Then for the first time a trust comes into being through the action of the statute, a trust coëxtensive in its subject matter with all the assets of the bank, irrespective of their nature, and yet a trust for a special class, the owners of negotiable instruments whose debts remain unsatisfied after payment of the paper has been collected by the agent. Cf. *Spradlin* v. *Royal Manufacturing Co.*, 73 F. (2d) 776. "Such owner or owners shall be entitled to a preferred claim upon such assets, irrespective

[6] "Sec. 13 (1) When the drawee or payor, or any other agent collecting bank shall fail or be closed for business by the state bank commissioner or by action of the board of directors or by other proper legal action, after an item shall be mailed or otherwise entrusted to it for collection or payment but before the actual collection or payment thereof, it shall be the duty of the receiver or other official in charge of its assets to return such item, if same is in his possession, to the forwarding or presenting bank with reasonable diligence.

. . . . . .

"(3) Where an agent collecting bank other than the drawee or payor shall fail or be closed for business as above, after having received in any form the proceeds of an item or items entrusted to it for collection, but without such item or items having been paid or remitted for by it either in money or by an unconditional credit given on its books or on the books of any other bank which has been requested or accepted so as to constitute such failed collecting or other bank debtor therefor, the assets of such agent collecting bank which has failed or been closed for business as above shall be impressed with a trust in favor of the owner or owners of such item or items for the amount of such proceeds and such owner or owners shall be entitled to a preferred claim upon such assets, irrespective of whether the fund representing such item or items can be traced and identified as part of such assets or has been intermingled with or converted into other assets of such failed bank."

of whether the fund representing such item or items can be traced and identified as part of such assets or has been intermingled with or converted into other assets of such failed bank." A trust so created, to arise upon insolvency, is a preference under another name. As applied to a national bank, the preference is plainly inconsistent with the system of equal distribution established by the federal law. R. S. § 5236; 12 U. S. C. § 194; *Davis* v. *Elmira Savings Bank*, 161 U. S. 275, 283, 284; *Easton* v. *Iowa*, 188 U. S. 220, 229; *Cook County National Bank* v. *United States*, 107 U. S. 445; *Texas & Pacific R. Co.* v. *Pottorff*, 291 U. S. 245; *Lewis* v. *Fidelity & Deposit Co. of Maryland, supra.* The power of the nation within the field of its legitimate exercise overrides in case of conflict the power of the states.

The decree is reversed, and the cause remanded for further proceedings in accordance with this opinion.

It is so ordered.

A true copy.

Test:

Clerk, Supreme Court, U. S.